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S. Hrg. 99-246, PT. XVIII

TAX REFORM PROPOSALS—XVIII

COMPLETED

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ORIGINAL

HEARING

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

JULY 24, 1985

LABOR LEADERS

S. Hrg. 99-246, Pt. XVIII

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Printed for the use of the Committee on Finance

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TAX REFORM PROPOSALS—XVIII

WEDNESDAY, JULY 24, 1985

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 9:30 a.m. in room SD-215, Dirksen Senate Office Building, Hon. Bob Packwood (chairman) presiding.

Present: Senators Packwood, Chafee, Bentsen, Moynihan, Baucus, Bradley, and Mitchell.

[The press release announcing the hearing follows:]

[Press Release, Tuesday, June 25, 1985]

TAX REFORM HEARINGS IN FINANCE COMMITTEE TO CONTINUE IN JULY

Examination of President Ronald Reagan's tax reform proposal will continue in July with a series of hearings before the Senate Committee on Finance, Chairman Bob Packwood (R-Oregon), said today.

"We made a good start on the hearing portion of this long process toward overhaul of the Internal Revenue Code during June," Senator Packwood said. "The hearings we have scheduled for July will take us further toward our goal of having a bill to the President by Christmas."

The hearing announced today by Senator Packwood include:

On Wednesday, July 24, representatives of America's organized labor unions will present their views to the Committee on the President's tax reform recommendations.

The CHAIRMAN. The hearing will come to order, please.

This morning is the 18th or 19th, or 80th or 90th—I have lost track—of a continuation of hearings on the President's tax reform bill, or variations thereof, and today we are hearing from a variety of labor leaders, including Lane Kirkland, the president of the AFL-CIO, on issues of immediate concern to them.

As I have indicated before, we will be continuing these hearings throughout the rest of this month, through most of September, and the first 2 or 3 days in October, and at that stage we will be in a position to move to a markup on a bill if we have recieved one from the House by that time.

Pat, do you have any opening statement?

Senator MOYNIHAN. I welcome our guest, Mr. Chairman.

The CHAIRMAN. In that case, we will start with Mr. Kirkland, the president of the AFL-CIO. As I have told all of the witnesses, their statements in full will be in the record, and we would appreciate it if they would abbreviate them orally so we would have time for questions.

Lane.

STATEMENT BY LANE KIRKLAND, PRESIDENT, AMERCIAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS, WASHINGTON, DC, ACCOMPANIED BY ARNOLD CANTOR FROM THE ECONOMIC RESEARCH DEPARTMENT, AFL-CIO, AND WALTER SLOCOMBE, CAPLIN & DRYSDALE, CHARTERED, WASHINGTON, DC

Mr. **Kirkland**. Thank you, Mr. Chairman.

My name is Lane Kirkland. I am president of the AFL-CIO, and with me today are Arnold Cantor from our economic research department and Walter Slocombe, who is representing us and assisting us in consideration of these tax issues.

Thank you Mr. Chairman, for this opportunity to present the AFL-CIO's views on tax reform generally, and the Administration's tax proposals specifically. Before proceeding, however, I would like to personally thank you, Senator Packwood, for your outspoken concern over the impact of the President's tax proposals on middle income working people and your opposition to the taxation of employee benefits.

The **Chairman**. Thank you.

Mr. **Kirkland**. We have a history of advocacy and support for a fair tax structure that goes back for generations. We believe Americans have a special interest in the fair tax structure and that our citizens deserve and seek both tax reform and tax simplification. Unfortunately, most Americans are convinced that tax legislation is crafted by special interests other than their own, and that avoidance and evasion is the name of the game.

This committee has the opportunity to develop a more simple, understandable, and equitable Tax Code. The AFL-CIO will fully support such an effort.

The President's tax proposal claims to meet these objectives, and a number of its features have merit. The AFL-CIO emphatically endorses, for example, the provision taking most poor Americans off the tax roles. As a package, however, the President's proposal does not add up to the major overhaul needed to establish fairness and end the preferential treatment given wealth individuals—stock and real estate speculators, oil and gas developers, and corporations.

We believe knowledge of these flaws and weaknesses has become widespread, and we hope the Congress will act decisively to improve the package along the lines that we will set forth in order to assure real tax reform.

Today the Federal income tax structure rests on a double standard that unfairly discriminates against one form of income—wages and salaries—in favor of unearned income which can be sheltered through phantom deductions, capital gains exemptions, phony losses, and overseas investments. By contrast, working men and women who pay the lion's share of taxes meet their income tax obligations in full every payday.

In our view, the key test of a tax reform proposal is the extent to which it diminishes unfairness toward people who work for their money and eliminates favoritism toward people whose money works for them. By that test, much of the President's program falls short.

We are pleased that the administration candidly acknowledges the need to correct some of the excesses of the 1981 corporate tax cuts, and recognizes that corporations have been less than forthcoming in funding even a modest share of the Nation's public needs.

So it is unfortunate that the administration has backed away from some of the more equitable of its earlier recommendations and retains some of its worst.

As this committee knows, the AFL-CIO strongly objects to taxing certain employer-paid benefits. We are pleased that the administration proposal continues the current law provisions applying to employer-paid legal education, group life insurance, and child care plans. However, we remain firm in the conviction that employer-funded health insurance should not be considered income subject to tax.

I have attached to this testimony an excerpt from my statement before the House Education and Labor Committee on March 21 which spells out our opposition to taxation of benefits. As for the taxation of unemployment benefits, worker compensation, and black lung benefits, such a proposal would simply heap further burdens on those suffering the loss of employment and the pain of work-related inury, disease, and even death.

Unemployment insurance benefits, which averaged only $119 per week across the Nation, are already subject to taxation if income exceeds $18,000 for married taxpayers and $12,000 for singles. At most, unemployment compensation replaces half of lost wages, while many States provide far less. Taxing the meager benefits provided under these programs adds injustice to hardship and indignity.

One feature of the administration's proposal is especially perplexing and objectionable: the attempt to do away with the deduction for State and local income, sales, and property taxes. This proposal has nothing to do with fairness, tax neutrality, or tax simplification; rather, it is a measure that will have far-reaching detrimental effects on many communities. The most severely hurt will be those States and localities that most conscientiously live up to their public responsibilities, or that have populations larger, older, poorer, or more disadvantaged than the average.

The recommendation to end the second-earner deduction is another antiworker proposal that is in direct conflict with the President's avowed pro-family sentiments. Eliminating this deduction recreates the marriage penalty and targets a particular group—working families—for tax increases. Moreover, in conjunction with other proposals in the President's package, this move would result in substantial tax increases for many young, small, working families who have been particularly affected by high interest rates and inflated housing costs.

Mr. Chairman, the steps that are needed to create an equitable tax measure cannot be taken within the confines of the three parameters established by the administration in this bill: Revenue neutrality, drastic cuts in tax rates on the wealthy, and the small shift in the distribution of tax burdens between corporations and individuals. To achieve true tax fairness, this package of constraints must be rejected.

The administration originally projected a 5-year revenue loss totaling less than $12 billion under its program. Since then, however, the Treasury, the Congressional Budget Office, and several private analysts have predicted far greater costs.

The budget cuts that the citizens of the United States have had to endure in the past few years and the continued high deficits do not permit any further revenue leakage through the Tax Code.

It would be the height of irony if the tax cut for those with $200,000 incomes were paid for by a cut in retirees' Social Security COLA.

In our prepared testimony we suggest ways in which the committee can shape a tax reform package that will move more decisively toward tax justice without the revenue loss of the President's proposal, and without increasing the taxes of the vast majority of Americans.

To bring true fairness in the overall package, we recommend changes on both the corporate and individual sides of the ledger. On the corporate side we urge the committee to reject the deep cut in the corporate tax rate, stengthen the corporate minimum tax, curb tax privileges of the oil and gas industry, establish a depreciation system that realistically reflects the cost and useful life of capital assets, change the foreign tax credit to a deduction, reject the administration's proposal for a 10-percent deduction for corporate dividends, use this opportunity to end the tax incentives for hostile takeovers and mergers.

With regard to individual tax reform, we believe that the Congress must scale back the sharp reduction in the rates for highest income individuals, consider paring the advantage given to high-income individuals through the proposal to increase the personal exemption, reduce further the availability of tax shelters, especially the use of large partnerships, establish an effective individual minimum rate, end the preferential treatment for capital gains, reenact the 1982 provision to require tax withholding on interest and dividends, reject the President's attempt to reduce employee job-related deductions, completely review the pension provisions of the administration's tax plan, retain Federal financing of Presidential elections.

Thank you, Mr. Chairman. The full statement I have offered for the record.

The CHAIRMAN. Thank you, Lane. You were right on the buzzer. having known you for 15 years, that is an amazing accomplishment. [Laughter.]

[Mr. Kirkland's written testimony follows:]

85-38

TESTIMONY OF LANE KIRKLAND, PRESIDENT, AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS, BEFORE THE SENATE FINANCE COMMITTEE ON THE REAGAN ADMINISTRATION'S TAX PROPOSAL

July 24, 1985

Thank you, Mr. Chairman, for this opportunity to present the AFL-CIO's views on tax reform generally, and the Administration's tax proposals specifically.

Before proceeding, however, I would like to personally thank you, Senator Packwood, for your outspoken concern over the impact of the President's tax proposals on middle income working people and your opposition to the taxation of employee benefits.

We have a history of advocacy and support for a fair tax structure that goes back for generations. We believe Americans have a special interest in a fair tax structure and that our citizens deserve -- and seek -- both tax reform and tax simplification. Unfortunately, most Americans are convinced that tax legislation is crafted by special interests other than their own and that avoidance and evasion is the name of the game.

This committee has the opportunity to develop a more simple, understandable and equitable tax code. The AFL-CIO will fully support such an effort.

The President's tax proposal claims to meet these objectives and a number of its features have merit. The AFL-CIO emphatically endorses, for example, the provisions taking most poor Americans off the tax rolls.

As a package, however, the President's proposal does not add up to the major overhaul needed to establish fairness and end the preferential treatment given wealthy individuals, stock and real estate speculators, oil and gas developers, and corporations.

We believe knowledge of these flaws and weaknesses has become widespread and we hope the Congress will act decisively to improve the package along the lines that we will set forth in order to assure real tax reform.

Today, the federal income tax structure rests on a double standard that unfairly discriminates against one form of income -- wages and salaries -- in favor of unearned income, which can be sheltered through phantom deductions, capital-gains exemptions, phony losses and overseas investments. By contrast, working men and women, who pay the lion's share of taxes, meet their income tax obligations in full every payday.

In our view the key test of a tax-reform proposal is the extent to which it diminishes unfairness toward people who work for their money and eliminates favoritism toward people whose money works for them.

By that test, much of the President's program falls short.

A tax structure founded on the principle of ability to pay should never have been allowed to add to the burdens of people living on the edge of impoverishment. While the President's tax proposals are helpful to poor people in the main, many are left out and some would face tax increases. For example, a working mother earning $15,000 per year with two children requiring child care has zero tax liability under present law. Under the President's proposal she could bear a tax burden of $135.

The impact would fall unevenly on middle income Americans with tax cuts going primarily to non-itemizers while those with deductible expenses will face tax increases. Although this legislation has been offered as a tax cut for most of the people, millions of middle income Americans will pay higher taxes while the vast majority of wealthy Americans will pay less. (See attached table for examples)

We are pleased that the Administration candidly acknowledges the need to correct some of the excesses of the 1981 corporate tax cuts and recognizes that corporations have been less than forthcoming in funding even a modest share of the nation's public needs.

The corporate tax share has been spiraling down since the mid-1950's, when business taxes financed a full fourth of the federal budget. Last year, when profits were booming, the corporate sector provided only 8.5 percent of federal tax revenues. It's hard to think of anything that does more to undermine taxpayer morale and confidence in government than the knowledge that dozens of giant, profitable corporations pay less in taxes than the lowest-paid employee who punches the timeclock.

So it is unfortunate that the Administration has backed away from some of the more equitable of its earlier recommendations and retained some of its worst.

As this committee knows, the AFL-CIO strongly objects to taxing certain employer-paid benefits. We are pleased that the Administration's proposal continues the current law provisions applying to employer-paid legal, education, group life insurance and child care plans. However, we remain firm in the conviction that employer-funded health insurance should not be considered income subject to tax. I have attached to this testimony an excerpt from my statement before the House Education and Labor Committee on March 21, which spells out our opposition to taxation of benefits, and which I will briefly summarize.

Most other industrial nations recognize health care as fundamental to a progressive, compassionate society and have chosen to fund such programs publicly through the direct support of general revenues. The U.S. has chosen, to date, to avoid a National health program and has chosen instead to meet its health care needs through a tightly administered system of tax deduction for the employer and tax exemption for the employee. Since 140 million people now have job-related health care, this is not a tax gimmick that benefits only an elite few or a narrow "special interest" group. We strongly fear that to tax these benefits is to begin the erosion of an established social policy without consideration of any alternative.

As for the taxation of unemployment benefits, worker compensation and black lung benefits, such a proposal would simply heap further burdens on those suffering the loss of employment and the pain of work-related injury, disease, and even death.

Unemployment insurance benefits, which average only $119 per week across the nation, are already subject to taxation if income exceeds $18,000 for married taxpayers and $12,000 for singles. At most, unemployment compensation replaces half of lost wages while many states provide far less.

Taxing the meager benefits provided under these programs adds injustice to hardship and indignity.

One feature of the Administration's proposal is especially perplexing and objectionable: the attempt to do away with the deduction for state and local income, sales, and property taxes. This proposal has nothing to do with fairness, tax neutrality, or tax simplification. Rather it is a measure which will have far-reaching detrimental effects on many communities. The most severely hurt will be those states and localities that most conscientiously live up to their public responsibilities or that have populations larger, older, poorer or more disadvantaged than the average.

Federal deductibility also serves as a device which blunts interstate and intrastate tax differences. Doing away with this deduction would make economic competition within and among states more severe.

Above all, this proposal would substantially undermine the ability of the states and localities to raise revenues at a time when the Federal government's financial policies are forcing terminations and cutbacks in programs of aid. For five years this Administration has built upon the concept of "new federalism" to shift responsibilities to the states. The states that have tried hardest to meet these responsibilities would be penalized and their tax base eroded under the Reagan proposal.

The recommendation to end the second-earner deduction is another anti-worker proposal that is in direct conflict with the President's avowed pro-family sentiments.

Eliminating this deduction recreates the marriage penalty and targets a particular group -- working families -- for tax increases. Moreover, in conjunction with other proposals in the President's package, this move would result in substantial tax increases for many young, small working families who have been particularly affected by high interest rates and inflated housing costs.

The proposal ignores the changing nature of American families. The Administration's concept of the "traditional" American family no longer applies. Two-earner families are rapidly becoming the national norm. In 46 percent of the families with children under age six, both parents are working; 67 percent of the mothers of preschool children are members of the labor force. Under the President's plan, two-earner families would lose the marriage deduction and they, and single parent families, would lose the child care credit and the deduction for taxes on their home. A working couple with one child, buying a home on a $35,000 income, could expect a tax increase of more than 20 percent.

Mr. Chairman, the steps that are needed to create an equitable tax measure cannot be taken within the confines of the three parameters established by the Administration in this bill: revenue neutrality, drastic cuts in tax rates on the wealthy, and a small shift in the distribution of tax burdens between corporations and individuals. To achieve true tax fairness this package of constraints must be rejected.

The Administration originally projected a five-year revenue loss totalling less than $12 billion under its program. Since then, however, the Treasury, Congressional Budget Office and several private analysts have predicted far greater costs. The budget cuts that the citizens of the United States have had to endure in the past few years and the continued high deficits do not permit any further revenue leakage through the tax code. It would be the height of irony if the tax cut for those with $200,000 incomes were paid for by a cut in retirees' social security COLA.

The AFL-CIO would like to suggest ways in which the committee can shape a tax reform package that will move more decisively toward tax justice without the revenue loss of the President's proposal and without increasing the taxes of the vast majority of Americans. To bring true fairness in the overall package, we recommend changes on both the corporate and individual sides of the ledger.

A fundamental factor in constructing a balanced and equitable tax system is to ensure that corporations pay their share of the tax burden. The 1981 corporate tax cuts generated enormous revenue losses, created a new industry around the buying, selling and leasing of tax writeoffs and opened gaping inequities among companies and industries and between individuals and corporations.

The President's tax proposal picks and chooses from a vast array of preferences, keeping some business subsidies and eliminating others. The result is not tax neutrality, but a continued distortion of economic and business decision-making. This action invites the kind of manipulations that have brought the current system into disrepute.

Moreover although the Administration claims corporate tax revenue will increase over the next five years, a Congressional Budget Office study concluded: ". . . the general corporate provisions included in the President's tax plan (depreciation rule changes, the Investment Tax Credits, the corporate rate cut, and the partial dividend deduction) will probably reduce the tax burden on income earned in the corporate sector in the long run." (Analysis of Long-Term Revenue Impact of the President's Tax Reform Plan, Staff Working Paper, June 1985 -- CBO)

We urge the Committee to take the following steps:

- Reject the deep cut in the corporate tax rate. There is no justification for slashing corporate tax rates by nearly one-third. Each percentage-point cut in the corporate rate from the present 46 percent to the proposed 33 percent costs the Treasury $2 to 3 billion yearly in revenue.

- Strengthen the corporate minimum tax. After many years of open scandal over the fact that major corporations whose profits total billions of dollars pay little or no taxes, bills have been introduced in both houses of Congress calling for a corporate minimum tax. Such a tax could raise as much as $23 billion in revenues over the next two years, while the President's proposal raises less than one billion dollars.

- Curb tax privileges of the oil and gas industry. The Treasury's November recommendation would have trimmed many unnecessary special preferences for the oil and gas industry increasing revenues by nearly $10 billion per year. The President's proposal trims oil tax reform to one-tenth of that amount.

- Establish a depreciation system that realistically reflects the costs and useful life of capital assets. The original Treasury proposal would have scrapped the 1981 accelerated cost recovery system (ACRS). The current proposal stretches out depreciation time tables to a lesser degree than the November proposal and includes basically a one-shot effort to prevent windfall tax benefits that would result from the combination of drastic rate reductions and previous depreciation schedules. The November Treasury proposal would raise $81 billion through depreciation reform in 1990 while the current proposal would raise only $21 billion.

- Change the foreign tax credit. While we support the President's proposal to restrict this subsidy to offshore production, we believe that additional measures are appropriate. According to IRS figures, in 1982 U.S. corporations claimed foreign tax credits in excess of $19 billion. We believe there is no reason to subsidize U.S. firms to invest and produce overseas. Foreign taxes should be considered as a cost of doing business exactly like state and local taxes and should, therefore, take the form of deductions, not dollar-for-dollar credits. Shifting from a credit to a deduction could recover as much as $10 billion a year in taxes.

- Reject the Administration's proposal for a 10% deduction for corporate dividends. This provision would merely provide this nation's corporations with roughly a $6 billion windfall tax break for doing something that they would do in any event: - distribute dividends to their shareholders.

- Use this opportunity to end the tax incentives for hostile takeovers and mergers. The current wave of corporate takeovers does serious injury to workers, customers and the community in which the target company is located. Workers and their communities too often finance the costs of the raid by job losses or pay cuts that cripple or destroy Main Street. The tax code in many cases abets this travesty, and the committee should remove all corporate takeover tax incentives.

We urge the Committee also to take these steps with regard to individuals.

- Scale back the sharp reduction in rates for highest income individuals. This Administration's tax proposals have consistently favored the wealthy. Since it took office the top rate has dropped from 70% down to 50% and now to a proposed 35% with a top capital gains tax rate of only 17.5%. The President's own figures show that individuals with incomes of $200,000 and up -- a group representing one-half of one percent of the nation's taypayers -- will receive over $4 billion of the tax savings. He proposes that this group receive 25% of the tax reduction, or an average of $10,000 each. This is another unfair reward to the wealthy. The 1981 tax bill gave large cuts to wealthy individuals. We urge the Committee to establish additional brackets to redress this inequity.

- Consider paring the advantage given to high-income individuals through the proposal to increase the personal exemption. The President's plan relies heavily on increases in the personal exemption to remove the poor from the tax rolls and offset the removal of many middle class deductions and exclusions. The value of the personal exemption, however, is considerably higher for wealthy individuals. A fairer system would ensure that the personal exemption is worth the same to all individuals regardless of income.

While the Administration plan makes some attempts to reduce the availability of tax shelters, it leaves many shelter opportunities intact. For example, it drops the provision in the earlier proposal to tax large partnerships (those with more than 35 partners) as the corporations they are in all but name. Instead, the current proposal preserves the main device of tax shelter promoters -- use of limited partnerships to pass through tax benefits to tax-motivated investors. This provision means that if there is a tax abuse to be enjoyed -- and the over-generous rules for depreciation, oil and capital gains insure that there will be -- there will be a way clever promoters can market and exploit it.

- Establish an effective individual minimum tax. In order to ensure fairness, the imposition of a minimum individual tax is necessary. Bills have been introduced to create such a tax that could raise $12 billion in 1986 and 1987 alone. The Administration's proposal on the other hand would raise only one-thirtieth of that amount over the same time period.

- End the preferential treatment for capital gains. The capital gains preferences are the most complicating features of the tax code and contribute most to the double standard which exists between earned and unearned income. Even though the President has proposed a modest reduction in the amount of capital gains that can be excluded from taxation (from 60% to 50%) the effective tax-rate on capital gains would actually be reduced for the wealthy taxpayers because of the tax rate reductions. We believe this is in direct contradiction to the concept of tax fairness. Ending this exclusion and taxing capital gains in the same manner as earned income could raise over $10 billion each year, even with the President's proposed slashing of the top tax rate.

- Reenact the 1982 provision to require tax withholding on interest and dividends.
- Reject the President's attempt to reduce employee job-related deductions. The imposition of a threshold on employee work-related expenses and other miscellaneous deductions will force individuals to add up a host of minor and major expenses to see if they meet the test for deductibility. This is hardly tax simplification; it complicates the tax filing process and directly burdens working people. It would eliminate such deductions as protective clothing, tools and union dues for many workers.

Carefully review the pension provisions. In general it appears that the Administration's proposals go in the direction of appropriate restrictions in order to prevent misuse and excessive benefits to higher paid employees. However, some of the rules concerning lump-sum distributions and early retirement pensions -- income averaging and excise taxes --could adversely affect working people. We also believe the abuses of present law in the employee leasing area must be corrected.

In addition, Mr. Chairman, we believe that the Committee must not turn its back on the Federal financing of Presidential elections, as the President proposes under the guise of simplification. This proposal has no revenue effect and involves only one line on the tax form. The suggested repeal represents nothing more than an Administration attempt to impose its ideology without the hearings and debate that preceded Congressional enactment of the federal financing law. We also oppose the elimination of the tax credit for political contributions.

Over the years, Mr. Chairman, the American labor movement has given a great deal of thought and study to the establishment of a fair, balanced and equitable tax system. We believe that such a system can be achieved in this 99th Congress.

We are well aware that there remains much work to be done. The suggestions I have made today are by no means definitive.

In the coming months, as you continue your review of the entire issue of tax reform and tax simplification, the AFL-CIO stands ready to participate in every way we can toward the development of a truly fair and equitable tax plan. We look forward to this effort, and we offer our wholehearted cooperation.

Attachment I

TAXES UNDER CURRENT LAW & REAGAN PROPOSAL
Selected Examples

Income: a)Total b)(Spouse)	Married/ Single Head of H.H.	a)Children b)Expense	City,State Tax Rate (Itemizers)		Itemize Y/N	Federal Tax			
						Current	Reagan	$ Ch	% Ch
1a) 14,000 b)(7,000)	Married	0	NA		N	891	945	+54	+6%
2a)15,000 b)NA	Head	a) 2 b)$4,800	NA		N	0 (1,296 Child Care Credit)	135 (4,800 Child Care Deduction)	+135	NA
3a)25,000 b)(10,000)	Married	2	U.S.ave.	5.9%	Y	722	763	+42	+6%
4a)25,000 b)(10,000)	Married	2	NY,NY	8.7%	Y	621	763	+142	+23%
5a)25,000 b) None	Married	2	NA		N	1,991	1,395	-596	-30%
6a)25,000 b) None	Married	2	U.S.ave.	5.9%	Y	1,107	763	-343	-31%
7a)35,000 b)(10,000)	Married	2	U.S.ave	6.0%	Y	1,630	1,770	+140	+9%
8a)35,000 b)(10,000)	Married	1	U.S.ave.	6.0%	Y	1,325	1,710	+386	+29%
9a)200,000 b) None	Married	2	U.S.ave.	6.2%	Y	39,944	33,810	-6,134	-15%

Assumptions Used in Examples

1. Taxpayers with incomes above $20,000 are assumed to invest the maximum amount allowed by law in individual retirement accounts. Taxpayers with incomes below $20,000 are assumed not to invest in IRA's.

2. Itemizers are assumed to have an outstanding mortgage balance of 2.2 times their wage and salary income and pay interest at 13 percent.

3. Itemizers are assumed to pay other consumer interest on a balance equal to fifteen percent of their wage and salary income at a 15 percent interest rate.

4. The source of state and local tax rates is "Tax Burdens for Families Residing in the Largest City in Each State, 1982." Advisory Commission on Intergovernmental Relations, August, 1984.

5. For itemizers no miscellaneous deductions are included.

7/16/85

ATTACHMENT II

EXCERPT FROM

TESTIMONY OF LANE KIRKLAND, PRESIDENT, AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS, BEFORE THE HOUSE COMMITTEE ON EDUCATION AND LABOR ON EMPLOYEE BENEFITS PLANS

March 21, 1985

On behalf of the AFL-CIO, I am grateful to this committee for providing the proper forum in which to discuss some of the implications of the proposal to tax employee benefits. While the idea has been raised ostensibly as a tax and budget issue, it is primarily an issue of basic national social policy, in which this committee has jurisdiction, interest and competence.

Beginning a century ago in imperial Germany, and universally since World War II, the industrial nations of the world have looked upon health care, education, retirement security and life, disability and unemployment insurance as fundamental necessities of a stable, progressive society.

Tacitly or explicitly, these countries have perceived that the national interest requires constantly rising minimum standards in each of these areas, and most have dealt with them through government programs financed through general revenues. In all of the countries that have chosen this path, such programs have been endorsed, maintained and expanded by successive governments, liberal and conservative alike.

The United States has chosen a different path. Instead of adopting a direct and universal life support system, the Congress chose to try to meet these needs primarily through the tax code, by encouraging the untaxed diversion of a part of each worker's wage or salary earnings programs and other programs specified by Congress from time to time to meet perceived social needs, such as child care and prepaid group legal services.

The success of this social policy is testified to by the fact that 140 million people now have job-related health-care insurance protection in the U.S. Thus, this is not a tax incentive that has benefited only a small, powerful minority or a narrow, special-interest lobby.

This network of protection was created under the leadership of the American trade union movement, through the institution of collective bargaining, but it has long since become deeply embedded in the nation's whole employment structure, not the least in the non-union and anti-union companies that hope, by offering generous benefit programs, to dissuade their employees from organizing.

It would be hard to overstate the role of this life-support network in developing the nation's economy. Its protection has given millions the sense of security and confidence to enter the marketplace and undertake commitments for long-term mortgages, college tuition loans, time-purchase agreements for cars and durable goods of all kinds. Lenders are no less strongly influenced than borrowers by the presence or absence of these protective programs. America needs more not fewer of these personal life-support programs.

Until the late 1940s, working people and their families lived with the constant fear that illness or disability would mean dispossession and impoverishment as well. Such is still often the case if the job-related life-support system is disrupted by unemployment, as we saw in the recent recession. To many families whose breadwinner was laid off or fired, the loss of health-care insurance coverage proved a greater blow than the loss of the job itself.

Some found that even a short hospital stay wiped out all their savings. Others, without insurance or cash in hand, were stopped at the hospital door and sent to public health facilities, putting a heavy strain on public resources.

With the experiences of the recent recession freshly in mind, Congress ought to be considering ways to strengthen the private life-support system rather than devising new taxes to undermine it.

The attack on employee benefit programs is taking place at a time of huge and deepening federal deficits. But the tax treatment of benefits is not the source of this crisis. The attempt to raise revenues by taxing workers' benefits and reducing their standard of living is patently unfair. Even after accounting for tax increases enacted later, three-fourths of the deficit is directly attributable to the 1981 tax laws, which lavished huge and uncalled for depreciation write-offs on the nation's businesses, while giving vastly disproportionate personal tax cuts to upper income classes. The revenue shortfall should not be met by levying additional burdens on working people and adding to the unfairness that has characterized economic policies of the past several years.

Taxing workers' life support benefits has been a part of this Administration's agenda since its earliest days. Health insurance, accident and life insurance, unemployment compensation, workers' compensation, day care, education programs, group prepaid legal plans - even pensions - are all on the hit list. The Bradley-Gephardt "fair" tax plan, it should be noted, also would tax employee benefits.

The administration and others who would tax benefits seek to justify this effort with the notion of equal treatment of similarly situated taxpayers. This would make some sense if applied to preferences and abuses motivated by tax avoidance with few, if any, redeeming features. Unfairness is epitomized by such abuses as expense account living, country club membership, and other questionable preferences that discriminate in favor of those at the top. Such practices have no social purpose, and certainly should not be encouraged by the tax code.

In contrast, the employee benefit programs under attack are not frivolous perks or gimmicks to shelter income. They don't generate phony losses or otherwise reduce the taxes of the privileged, but are widely distributed in the national interest.

It is unfair that all workers do not benefit by an adequate medical program, pension protection, life insurance and other benefits. But such inequities should be resolved through public and private policies that encourage a leveling-up of benefits not by policies that seek to reduce everyone to the lowest common denominator.

Such a narrow view of equity ignores the far greater inequity that would result from a lowering of benefits and fewer participants. That viewpoint also implies that tax justice means merely rearranging the tax burdens of working people.

To qualify for tax exclusion now, benefit plans must comply with stringent rules that prohibit discrimination in favor of owners, officers, shareholders and highly compensated employees and generally contain limitations and constraints to assure that the intended beneficiaries and purposes are served. That test clearly distinguishes these provisions from so many other so-called tax preferences which primarily benefit a privileged few and provide no assurance that any national purpose will be served.

Far more important, if tax fairness is a concern, is the equity that could be achieved through closing the many loopholes and distortions in the tax code that now heap the burden of taxation on working people as a group and tread only lightly on corporations, wealthy stockholders, investors and speculators.

Those who would tax employee benefits also like to link the growth in benefits to the tax code as if workers and employers were conspiring to raid the Treasury.

But a review of the origin, growth and structure of workers' benefits destroys this notion.

A recent Library of Congress study of employee benefits discusses the many reasons for their growth and underscores their social purpose. Among other things the study points out that as living standards rise, workers rightly become more concerned about the economic consequences of death, illness or unemployment and give up wages and other improvements to gain security through essential protections. Employee benefit programs also generate "economies of scale" that reduce cost. The effects of benefits in reducing worker turnover and promoting employment stability as well as the role of unions in raising the level of benefits are highlighted. The study notes that unionized firms have an average of 30 percent higher levels of benefits than comparable nonunion firms.

The analysis also points out that even with the dramatic increases of benefits in the post-World War II era ". . . the relative level of U.S. fringe benefits still remains a smaller part of total compensation than it is in most other industrialized nations."

In exempting health insurance contributions from taxation, the Congress has promoted private health coverage and lessened the need for a comprehensive public health program. Subjecting such health contributions to taxation would inevitably undermine private coverage and require a greater direct public role and increased expenditures for the provision of health care.

If tax benefits for health care contributions were to be scaled back, most likely to be dropped from a benefit plan are coverage for preventive care, outpatient diagnostic services, dental, eyeglasses and other benefits that affect premium costs but have little to do with the health cost inflation problems that plague the nation, primarily in doctor and hospital fees.

In advocating the employee health tax, the Administration would have citizens believe that health care is a costless "fringe" to workers. In fact, tough economic decisions are made and other benefits, including wages, are sacrificed to preserve and enhance the health care benefit package. All of us are extremely sensitive to the rising costs of health care services and, in collective bargaining, increasingly have had to make difficult decisions in the absence of comprehensive cost-containment legislation to reduce the rate of growth in total health care costs. This has obviously resulted in a growth in health insurance benefits relative to wages and salaries. The rising expenditure on medical care has increased from 3.2 percent of GNP in 1953 to 7.2 percent in 1983. This rise reflects greater citizen use of medical care, the increasing quality and availability of treatments, and the rapid increase in the cost of medical care. Increased costs and usage have little relationship to the fact that employee medical benefit plans are not taxed. In fact, there has been a rise in the number of plans that require employees to pay a portion of the health insurance costs -- an occurance in direct conflict with the notion that the tax exemption has caused the increased use.

The Administration also has claimed that health insurance benefits are unnecessary subsidies for higher wage workers. The AFL-CIO strongly rejects this position.

Employers contribute the same amount for health coverage per employee, regardless of income. As a result, health benefits as a percent of income are more valuable to families at lower wage levels. Limiting tax free contributions would, therefore, place a disproportionate burden on middle- and lower-income workers who would find it much more difficult to maintain their level of benefits.

The next step is obvious: The young, the single and the poor, if given the opportunity, would be inclined to opt out of their plans. Those left would be those who can afford the higher costs and those who are older and more in need of frequent health care services. This in turn will cause the premiums of the plan to go up, raising taxes further.

Unemployment Assistance and Workers' Compensation

Without question, the most mean-spirited aspect of the Administration's proposals to tax life support benefits involves the heaping of further burdens on those suffering the loss of employment and the pain of work-related injury, disease and even death. Taxing the meager benefits provided under unemployment insurance or workers' compensation adds to the injustice for those workers who have experienced the indignity of job loss or the tragedy of injury or disability stemming from the workplace.

Unemployment insurance benefits, which average only $119 per week across the nation, are already subject to taxation if income exceeds $18,000 for married taxpayers and $12,000 for singles. The Treasury proposal would tax all UI benefits. In 1980, the National Commission on Unemployment Compensation, comprising of representatives of employers, workers and the public, recommended the "repeal of current provisions under which a portion of UI income is taxed." In its report to the President and the Congress, the commission said, "UI is the first line of defense against extreme hardship caused by unemployment. When a person is unemployed, the family's income stream is already reduced even if UI is being received. To subject this family's reduced income stream to income taxation adds to the unemployed person's sense of injury already caused by the loss of a job."

Just as devastating is the suggestion by the Administration to tax all workers' compensation benefits. At most, workers' compensation replaces two-thirds of lost wages. Caps and ceilings in many cases mean even less protection. The 1972 National Commission on Workmen's Compensation Laws concluded that, in general, inadequate benefit levels and inequitable treatment existed in all states. The 1979 report of the Interdepartmental Workers' Compensation Task Force found that by the most conservative standards, workers' compensation cash benefits to impaired workers were seriously inadequate. In the face of these authoritative studies, the Treasury now wants to make a bad situation immeasurably worse by taxing these benefits and further widening the gap between net income levels and what is necessary to maintain decent living standards.

Conclusion

In conclusion, I would again like to commend this committee for holding these hearings on employee benefits. These life support benefits are an important part of our nation's social policy and must not be relegated to the narrow confines of the tax code. Therefore, it is particularly gratifying that this committee is conducting this investigation.

Four decades ago, few of America's working people enjoyed these benefits. Today, because of such factors as the decisions of the Congress, court decisions, collective bargaining, and the higher wages that have allowed workers to devote more of their income to health and welfare, a large portion of both union and non-union workers receive a variety of life support benefits. The intent of Congress was clearly to promote the spread of these programs.

Largely because of the revenue shortfall created by the unfair and revenue-eroding Tax Act passed in 1981, these programs are being eyed as a source of new tax receipts. Nearly three-fourths of the deficit is directly attributable to the unfair revenue giveaways enacted in 1981. The nation can best resolve the deficit by reversing some of the real inequities in the tax code, not by levying additional burdens on working people.

The AFL-CIO strongly urges the members of this committee to resist the proposals to penalize workers and retard privately financed programs that promote social improvement and the well being of the American people.

The **Chairman**. You suggest a fourth bracket for the higher income earners; they are at 50 percent now, although, as we are all aware, the effective rate for most high income people is significantly lower than the maximum. Do you have any particular suggestion as to where the bracket ought to be? Are you suggesting below 50 but above 35?

Mr. **Kirkland**. Yes. I have no fixed figure in mind.

The **Chairman**. Every time we go through a tax reform, whether we are increasing the upper brackets or lowering the upper brackets, clearly those at the top of the bracket, if we raise it, have their percentages go up more when we are raising it than the lower income do, and when we come down they have their bracket percentage reduced more than those in the lower income bracket. Is there a way that we could somehow figure out what a fair level of tax is, hopefully excluding from the Federal income tax all of those below the poverty line as there is no reason why they should be paying income tax, but trying to figure out what a fair rate is for the rest of the public and somehow avoiding the argument of who gets their taxes raised or lowered more, using only as a base what the tax rate happens to be at the moment, which may be wrong?

Mr. **Kirkland**. Well, that would be a great ideal? Senator. I think the question has to be examined in the light of the revenue needs of the country at a given time and the economic condition of the country. The end ought to be to find a way to share those burdens most equitably.

No one is for taxes for their own sake; taxes are a burden. They are an obligation of citizenship. And I think what is fair in absolute terms, in terms of what the rates should be, could vary in terms of both the economic situation and the fact that we are confronting an enormous deficit, and the consideration also of the fact that if there is to be an element of the population that ought to be given special consideration in times of assuring fairness, it is those people who work for a living and are looking only for a simple life, to keeping their families together and food on the table and shelter over their heads and to send their kids to school, and not those who have an awful lot of room to spare in accomplishing those objectives.

I think those who have benefited the most from the fruits of a free society, a democratic society, ought to be prewpared to pay a larger share of the load.

The **Chairman**. I don't think anyone here or in the House of Representatives, man or woman, Republican or Democrat, disagrees with that concept—well, maybe some do, but very, very few do.

I know the House is toying with a 40-percent bracket. But at a 40-percent bracket the same argument can still be made, "those making over $200,000 will still benefit greater, percentagewise, than those at the bottom." I haven't figured it out, but my hunch is that even at a 45-percent bracket the percentage drop might be greater. And I don't know how to overcome that argument if at the same time you are trying to bring the rates down for everybody. You can't overcome it; it is just the inevitable result of starting with a high tax rate.

Mr. **Kirkland**. Well, there was a time, of course, in this city when the marginal tax rate was, I believe, something slightly over 90 percent, and those in the marginal brackets have seen their taxes come down far more drastically in terms of their last dollar earned than other lement of society. As I don't think there is an overwhelming argument for moving that marginal tax rate very substantially down. It was moved from 70 to 50 within recent years; that is a very substantial cut.

The **Chairman**. Lane, let me go through you, in very specific steps, how we came to this tax on the floor on health insurance benefits.

Mr. **Kirkland**. Right.

The **Chairman**. And I want to say this for the benefit and others, so no one is misled: Lane and I have been close friends for 15 years, and I talk with him frequently about matters involving more than just labor relations, and I talked with him to some extent about the issue of the taxation of employee benefits in attempting to broker a compromise between the administration and labor and, frankly, most of industry who is concerned with this issue. And my views on this are no secret—I don't think any of these employee benefits that are major social benefits should be taxed. I am not going to get into an argument about van pooling or something else; but health insurance, pensions, legal insurance, day care, the basic benefits that the every day Jane and Joe need to barely keep body and soul together I don't think should be taxed.

We were faced in Treasury One with first a health cap tax, and my hunch is that cap never would have been raised, and, as inflation went on, it would have been a greater and greater tax on health insurance benefits.

We were faced with the fact that both the present tax-free status of education provided by employers and prepaid legal provided by employers terminated at the end of this year. It sunsets, goes out of existence, unless the law is extended. And they would be fully taxed from dollar-one.

And the administration also was recommending—I shouldn't say "the administration." Treasury One was also recommending that the $50,000 in life insurance that employers provide and any day-care benefits that employers provide would be taxed from dollar-one.

At that stage, or in many stages, I called Mr. Kirkland; but I specifically want to recall the day when I called you about 10 in the morning and I said—and you correct me if I am wrong—"Lane, we are in the bind on this. The administration is very intransigent, and they want to stick with their health cap. And we are going to lose a lot of other tax-free benefits that are critical." Am I OK so far on what we talked about?

Mr. **Kirkland**. Absolutely.

The **Chairman**. It was about 10 in the morning.

Mr. **Kirkland**. That's right.

The **Chairman**. You called me back about 3 that afternoon. Can you relay what you suggested at that time? This wasn't a commitment—I don't mean that you were going to support the bill, but what you suggested at that time.

Mr. Kirkland. Yes, I suggested to you, sir, that in your discussions with the Treasury—and I want to make it quite clear that I encouraged those discussions. To me, at a time when the Treasury Department seemed determined to plant in this package some sort of a poison bill dealing with health insurance fringe benefits, it would have been the height of irresponsibility not to attempt to limit the damage as best one could.

In the discussions with Treasury I suggested that the best way to resolve it would be to add a line on the return——

The Chairman. These were in the discussions with me that afternoon.

Mr. Kirkland. That's right.

Add a line on the return. If you have an employer-paid health plan, $100 is added to your income for tax purposes, for a single family, all inclusive, max $100. And that was the burden of our conversation.

The Chairman. But it was part and parcel of an arrangement that Treasury would then back off of its attempt to tax education, legal, life insurance, and day care, wasn't it.

Mr. Kirkland. That is absolutely correct, sir.

The Chairman. And that was to be part of the arrangement.

Mr. Kirkland. That is right.

The Chairman. And then about an hour later you called me back because you wanted to make sure I understood, and you said, "Now, listen, that's $100 added to gross income, not $100 tax." And I said Yes, I understand that.

The administration's $250, that was their idea, and neither you nor I ever discussed that. And their $10 a month rather than $100 a year was their idea.

Mr. Kirkland. That is right.

The Chairman. We were not part and parcel of that. That is an arrangement that I suggested to Treasury, and that is where we are now. They have added a little more to it than we would have added on the $250, but that is how this arrangement came about. And I make it clear again that Mr. Kirkland has never said that he liked that arrangement; I don't like that arrangement.

Mr. Kirkland. I want to make it clear. I don't think I at any time ever suggested that I regarded any taxation of health insurance benefits as fair or just, and that we continued our resistence to that proposition.

The Chairman. Absolutely. And I indicated I didn't like them. And I was trying to figure out a way, in terms of these basic benefits, to get the best possible deal we could for the average working man and woman in this country.

Mr. Kirkland. To me it was an exercise in damage control in terms of the Treasury's position.

The Chairman. All right. I appreciate that, and I have no more questions.

Senator Moynihan?

Senator Moynihan. Mr. Chairman, you opened on a philosophic note about what is a fair tax, and I think Lane Kirkland made an important point. He observed that one asks that question by starting out and saying, "How much money do you need?" And then "who will provide it?"

Just for the record, over the weekend the press reported that we had long discussions about how this great deficit—that is such a problem for us all began, and there are those who have insisted that there was a deliberate strategy by the new administration to use the budget reconciliation process to dismantle social programs. This argument was not necessarily disputed by those involved, although not everyone agreed or could be persuaded that anyone would be crazy enough to try something that risky.

Frederich von Hyack, formerly a senior economist with the administration, gave an interview in a magazine in Vienna. He said he was disturbed about the deficit because it meant that the savings from all over the world had to come into the United States to pay for it, raising the price of capital. But he did say that the President's associates had explained to him that the deficit was necessary as a device to force Congress to cut out social programs. I will get it for the record, but if Frederich von Hyack says it, it must be so. I think that is the rule downtown, and we have it on the record.

I mention this because of a matter that Lane Kirkland knows concerns a lot of us, and a lot of trade unions—the elimination of the deduction for State and local taxes, which would have a devastating effect on education, increasing the real costs of education by 40 percent.

You know, I don't think there is an institution in this country that has had more experience with the problem of states competing for economic advantage by maintaining low levels of social provision for education, health, safety, and, for that matter, the right to organize and bargain collectively. And in more recent years you have found yourself dealing with the same subject internationally. And in the main, the history of this country has been to resist this at the national level, to try to have uniform standards.

Don't you see something of this returning? I mean, the deductibility of State and local taxes has mutated this competition; it becomes all-out and fierce in the absence of that deduction.

Would you speak to that point?

Mr. **Kirkland**. You are quite right, Senator. I think it would aggravate a problem that is already acute in this country, and that is the steps and measures that States will take I think against, in many cases, the best interests of many if not the majority of the people in those States to attract industry. It will increase that tyrannical exercise, and I think to the detriment of the strength of the country as a whole.

You know, I was struck by, or rather I must say a little bit startled, when the President visited a couple of States and spoke in a manner that was highly critical of those States that to my way of thinking most fully accepted the burden of providing for the general welfare of their population and who dealt with so many of the social problems that were wished on them or dumped on them, in effect, in many cases by other States, and other countries. And it seemed to me that the last President who traveled on the basis of denouncing one part of the country or one group of States as against another was President Jefferson Davis. And it doesn't seem to me it is wholesome for this country to return to that proposition that divided the country in that manner.

We are concerned, deeply about this. I can't help but recall some of the peregrinations that have taken place on this issue, and this issue in relation to the revenue needs and demands on the budget and expenses of the Government.

I recall having an argument with Joe Pechman in the last year of the Johnson administration. Joe Pechman and Walter Heller were the authors of something called the Heller Plan, which was a scheme that ultimately developed under the Nixon administration for revenue sharing. The rationale for revenue sharing—and I must say we opposed it at the time—offered by Joe Pechman, and I think he would probably confirm this if you asked him, was that the country faced a terrible problem, and that problem was the prospect of a mounting Federal surplus. That created a problem.

Senator **Moynihan**. "Fiscal drag" it was called.

Mr. **Kirkland**. Economists invented a term for it known as fiscal drag.

The deleterious consequences on the economy of a mounting Federal surplus was foreseen, and I saw the figures that were projected, because of growth and inflation—modest inflation at that time and rather strong growth. This was seen as a method of disposing of that surplus and helping the States by distributing the largesse of the proceeds of that growth and inflation to the States. It was not pursued by the Johnson administration, but it was taken up by the Nixon administration in the form of the original revenue sharing scheme, which was the basis and I think the burden of the so-called New Federalism at that time.

Now, we have come an awful long way from that concept. We have already, of course, dismantled in large part or are in the process of dismantling revenue sharing, which is a process by which the Federal Government shared a portion of its revenue with the States. And now we have the mirror opposite concept that is coming in that the Federal Government has to tax the revenues of those States for its fiscal needs. I think both in terms of concept—it is backward—and in terms of its practical consequences it is exceedingly dangerous.

Senator **Moynihan**. Thank you very much.

The **Chairman**. Senator Bentsen.

Senator **Bentsen**. Thank you very much, Mr. Chairman.

Lane, good to be with you this morning.

There is no question but what your criticism of this bill, insofar as it is doing more for very hign income than middle income is correct. But I have some question about adding a fourth tier to the tax level. It seems to me that there are better ways to handle that.

An example is reducing capital gains from 20 to 17.5. That obviously affects those making over $200,000 in a material way. That picks up a substantial amount of income if it was left at the 20.

Then the question of personal exemptions and the application of those at the higher levels, and some modification, also picks up some.

But it seems to me those are more appropriate than a fourth level.

Now, one of the arguments has always been that you get the rate down and you can not have as much attraction to tax shelters, and that hasn't worked as well as many had hoped when we went from

70 to 50; but at some point it has to apply. It would seem to me that that argues for trying to keep the top at 35 and making the adjustment in the other areas. You can pick up the money just as quickly there and still have the incentive to try to keep them away from the tax shelter. Would you comment on that?

Mr. KIRKLAND. Yes. I agree with your view on those two items, on revising the proposed individual exemption so as to confine its major effects to those for whom it is primarily intended, without it becoming an added boon to those in the high brackets, and the treating of capital gans in the same manner as other forms of income. I don't think those are mutually exclusive. we would favor those and the added bracket. I think that revenue will be needed, particularly in the light of our position that this proposed taxation of State and local government's ought to be changed.

Senator BENTSEN. You know, you were talking about the rate at one time having been higher.

I can remember one time in the Korean war when it was 94 percent, if I recall. I remember Ways and Means met one day and decided thay were going to put on a 10-percent surtax, and that would have meant you would have gone over 100 percent. They finally corrected that one.

The other point that you made is the question of the dollar check-off. I must say to my Republican colleagues, they have done an incredibly good job in fundraising, much better than we have on the Democratic side. I compliment them on it, and I envy them in their success. But it seems to me that it is terribly important in a Presidential campaign, to the extent you can, that you level that playing field insofar as the financing, and in addition to that, that the candidates have more time to speak to the issues instead of fundraising. I would like for you to elaborate on that point; you had only one paragraph here.

Mr. KIRKLAND. Yes. Well, the step that was taken with the dollar check-off was a move in the right direction in terms of election financing in this country. We think it is only a partial step. It addressed, of course, the national elections, and that is very important and has made I think a considerable difference for the better. It has labeled the playing field to some extent, and that is an objective that every citizen ought to embrace.

The President's proposal to eliminate it goes in exactly the wrong direction; in our view, a strong view, we need to take further steps. This is just the beginning. We need to take further steps in terms of eliminating or reducing the role of private wealth in campaigns, both at the Presidential level and at the congressional level, and at the local level.

Senator BENTSEN. I see my time has expired. Thank you very much. Mr. Chairman.

The CHAIRMAN. Senator Mitchell.

Senator MITCHELL. Thank you, Mr. Chairman.

Mr. Kirkland, I noted with interest your comments on the fairer distribution of the tax benefits, including a fourth bracket at a higher level and a change in the personal exemption.

When Secretary Baker was before the committee, I told him that I was in the process of preparing a possible amendment to accomplish the same purpose which had both of those points and a third point which was to increase the standard deduction.

One sentence in your written statement interests me, and I am going to read it and then ask that you submit in writing to me and the committee some further detail on it, because it may be helpful to me in that regard.

With respect to the personal exemption you said, "A fairer system would ensure the personal exemption is worth the same to all individuals regardless of income."

Mr. KIRKLAND. Yes.

Senator MITCHELL. I would like to have a written statement from you on that setting that forth in some detail.

Mr. KIRKLAND. We would be very happy to provide that, Senator. There are a number of ways of achieving that, as I am sure you understand.

To prevent this windfall to the well-off and retain the positive effects of the increase on the poor and middle class, the Committee should require taxpayers at the 35 percent rate to take the $2,000 personal exemption at the 25 percent rate. This would limit the tax benefit to $500 per exemption.

Senator MITCHELL. I am considering an amendment that incorporates those three elements—a fourth and higher bracket, a modification of the increase in the personal exemption, and an increase in the proposed increase in the standard deduction, all of which will, when taken in the aggregate, have the effect of shifting the benefits of the reduction away from those at the higher income levels into the middle-income levels, which is my objective and I believe is yours as well.

Mr. KIRKLAND. Yes.

Senator MITCHELL. Now, one other area that has interested me is the question of the tax on health insurance benefits. I noted with interest your exchange with the chairman about the genesis of this new proposal.

The original Treasury proposal, and let's limit to talk about families on an annual basis—there are families and single persons monthly and annually—the original Treasury proposal would have exempted the first $2,100 of value in health insurance benefits for families, and then subjected any amount in excess of that to tax.

The new proposal, by contrast, imposes a tax on the first $300 received by any such family. Now, with all due respect to you and the chairman, I understand the origin of this conversation. I cannot for the life of me see why it is more fair to tax the first $300 than it is to tax any amount in excess of $2,100. It seems to me that in the first place you are ensuring that every working person is taxed under this proposal, as opposed to the original one which would have taxed only those the value of whose benefit plans exceed $2,100. And second, this new proposal doesn't make any sense as health policy; whereas, of course, the first one did, at least in terms of making people sensitive to the implications of these expensive plans.

I wonder if you could tell me why you think it is better? I understand you are not for it, that you are against any tax; but what you said to the chairman is that this proposal is less bad that the other. I must say that I cannot understand why you think it is less bad than the other, and I wonder if you would explain that to me.

The **CHAIRMAN**. Could I add an addendum there, though, before he answers it? Don't forget that, absent a compromise, all employer-paid education, daycare, the prepaid legal plans, and the life insurance now provided was going to be taxed from dollar-one under that administration plan. And as I looked at it, the average individual was going to end up paying more taxes under that plan than they pay under the current arrangement we have come to. We weren't looking at this just in the context of health insurance alone.

Senator **MITCHELL**. I accept that, Mr. Chairman.

Would you go ahead, Mr. Kirkland?

Mr. **KIRKLAND**. Let me make several points. The first point is the point I made in response to Senator Packwood. I want to reiterate our deep conviction that there is no just and fair and sound basis for taxing these benefits at all; they should remain untaxed.

In terms of discussion with the Treasury, I also want to point out my position was a flat $100, not $300, and one-third is a substantial difference.

Senator **MITCHELL**. But the administration proposal is $120 for individuals as compared to $100.

Mr. **KIRKLAND**. Well, I am talking about my positions. I have not embraced the administration proposal; I want to make that exceedingly clear. I think the level is excessive.

The other point—the administration proposal is loosely described as putting a cap. It does not put a cap; if you are talking about taxes, there is ni cap. It is the total absence of a cap. If there is going to be taxation, which I oppose in this field, it should be finite, it should be simple, and the damage that it does to the bargaining process and the evolution of health plans should be minimal.

There is no cap on the Treasury One plan. The future inflation in the health costs and in the insurance premiums would be exactly translated into higher taxes, year by year, so that people covered by these plans would be continually having their taxes racheted up by inflation.

Second, it would involve a penalty on the bargaining process and on the evolution of these plans. That is to say, it would restrict the evolution of them by penalizing levels of benefits, premium rates above a certain level. Now, that would go precisely against what I think is our objective—certainly our objective—to improve and extend these plans and make them more comprehensive.

Just taking the two plans and a measure of their differences—and I repeat, I think the $300 family level in the administration plan is execessive—the difference in revenue between the two in Treasury One by 1990 is $24 billion, in Treasury Two $6.9 billion. So it is hard for me to say in the light of those figures how one can conclude that one that extracts from these plans $24 billion is more generous than one that extracts $7 billion, or better for the people covered by this.

Now, even taking Treasury One, that would have taxed all premiums over $175 a family. We have checked a few of the plans that are in effect. In the auto industry, that would have increased the income subject to tax by $1,620, and in steel by $672, for a machinist in Boeing by over $1,000, for oil workers in Shell Oil by $1,500, and that is just the beginning.

The **Chairman**. And that is not the total amount of the plan; that is how much you would have subject to tax. That is above the cap. That was above exemption.

Mr. **Kirkland**. The $175 a family.

Now, there are several other questions that remain unanswered that would have a rather profound effect on this. There are a great number of workers and families that have two earners. It is unclear to me how this bill proposes to treat that in tax terms. It is quite unclear to me. I have heard arguments on both sides. I suspect it would wind up being written by a GS-15 in the form of a regulation, and I would have some apprehension.

Now, that means, let's say, a worker, a wife who is working in a garment shop and has a health insurance plan that is below the cap, what they call the cap, the $175 per family, and she is married to someone who has another plan that is at or above the cap. That means, if you interpret their proposal to mean that those things are combined for tax purposes, it means that the entire premium for one worker would be subject to the tax, even if that plan itself is below that level.

There is a question of interpretation on composite premium rates, composite contribution rates. It is not clear to me how that is constructed. You know, there are millions of workers under plans where the negotiation calls for a 5 or a 6 percent contribution to health and welfare funds. What is the premium rate? What is taxed under this? I don't know. Do you go in and analyze that group, or how do you determine that for purposes of reporting? If you talk about simplicity, that isn't going to be simple.

So it is all the balance of things that would lead me to the conclusion that you questioned me about.

Senator **Mitchell**. Well, may I just make a concluding comment, Mr. Chairman?

It seems to me, after looking at it carefully, that probably the most appropriate mechanism, if one is enacted—that is the same context in which you suggested the $100—is to combine the two elements of an exemption of some level with the imposition of a tax on the excess, and a cap on the amount to be taxed. If you are going to deal in an area that has profound effects on health policy in this country, it seems to me that some consideration ought to be given to that effect, particularly since this committee has jurisdication over health matters.

And I would ask, with the resources you have and the suggestions which you have made here, if you would submit to me some suggested proposals that combine those two elements, that exempt a certain level from tax.

You see, you talked about the steel workers and the auto workers, who obviously have the best plans, but there are a lot of people working in other areas at far lower wages with far less valuable plans who might not have been taxed under the initial proposal but who will be taxed under this proposal. It seems to me we want to give some consideration to them as well. One way to do it would be to devise a mechanism, if it is possible, and I don't know that it is, that would have an initial exemption with an amount above that subject to tax but a cap on that amount as well.

The disadvantage of the administration's plan, as I gather from your standpoint, was that there was no cap on the amount subject to be taxed, the cap was on the amount of benefits that would be received without tax.

I wonder if you would do that?

I apologize, Mr. Chairman, for taking up so much time.

Mr. **Kirkland**. Well, that can be done. I wat to emphasize that is not what we favor. I am testifying here in opposition to the taxation of these benefits. I do not believe they should be taxed, and that is the simplest way of dealing with it.

Senator **Mitchell**. Well, I understand that; but you once made a suggestion to the chairman about an alternative proposal, even though you didn't favor it. I will ask you to make another one, even though you don't favor this one. [Laughter.]

[The proposal follows:]

A technique whereby caps and floors could be combined would be to exclude from income an amount up to a certain threshold, include as taxable income a percentage above that threshold, and then place a maximum on the total amount of income to be added.

The **Chairman**. Let's go through those figures again. In 1990, had we gone with the original Treasury bill, your estimates are that employee benefits would have been taxed to the tune of $24 billion, all benefits.

Mr. **Kirkland**. That's right. Yes.

The **Chairman**. The compromise we worked out—and I shouldn't say we, because you never did like it, but it ws a better compromise—would tax them in 1990 about $7 billion.

Mr. **Kirkland**. Which, from a standpoint of either/or, if those are your two choices, $7 billion is not as bad as $24 billion.

Mr. **Kirkland**. I hope there is a third choice.

The **Chairman**. I hope there is a third choice, I agree with you. But this is what intrigues me: Those that are most opposed to the floor tax that we have worked out are those who want to go back to what the Treasury proposed last November. There are members in this committee, there are Members in this Congress and in this Senate who want to tax employee benefits—all employee benefits—from dollar zero; health, daycare, legal, it doesn't matter what it is. Allegedly it is all earned income, and, "You ought to pay a tax on it." I don't suggest that. You don't support that. You have never suggested you supported that.

I hope that we get by with no tax at all. If we can't do that, I am going to work out the least possible tax; but I hope we get that third alternative.

Mr. **Kirkland**. Thank you, Senator.

Senator **Mitchell**. Well, I will try, Mr. Kirkland.

The **Chairman**. Mr. Kirkland, if by chance tax reform comes a cropper, and all we could get would be an effective minimum corporate and an effective minimum individual tax, would you support that?

Mr. **Kirkland**. Yes.

The **Chairman**. Second, tax neutrality. Can you elaborate a bit on your position on that? In your statement you certainly give the hint that you think the time may come when we need increased revenues, and that tax neutrality in and of itself should not be the holy grail.

Mr. **Kirkland**. Yes; in fact, we have, each year, at the time that the President sends up his budget message, proposed an alternative, and we have consistently proposed alternatives that would reduce the deficit substantially. I would particularly recall to mind a proposal that we made, put forward at the time that the first budget was sent up with a very large increase in the defense budget, concurrent with a proposal for a massive reduction in taxes, a program that in our view was heavily weighted on the upper end of the scale. We stated and declared at that time, and I said it repeatedly, that nothing could be more (a) damaging to the social fabric of the country, and (b) nothing would be better calculated to undermine and destroy the consensus and support of some defense buildup. I think that has been borne out be events.

We proposed, we said, that if there is a need for an enhanced defense spendng, then it ought to be paid for. It ought to be paid for on a current basis, and nobody should be exempt, and that the deadliest proposition that could be put forward was the proposition that, yes; the country is in danger and it needs more defense; but certain favored elements of the population, including those who have derived the most from the benefits of a free and democratic society, are not going to have to answer that summons, are not going to be drafted, they are going to be 4-F in the dealing with the costs of the expenditures necessary for the security of their country, including their own security and their own treasure. We thought that was a terribly dangerous and damaging proposition, that, "Yes, the country is in danger, we need a defense buildup of extraordinary proportions; but, Mr. Fat Cat, you are exempt; you are not only exempt, you are going to get a tax cut simultaneously." I think that was wrong, and I think we are paying the price for it right now. I think the people who have responded to the proposition that, "Yes, we have got to build up defense, and it has got to be paid for."

And we proposed that it be paid for. We proposed at that time, and repeated it in subsequent years, that when the Congress ascertains what the essential defense needs of this country are, and proposes an increase in those expenditures, that they should also propose a method of paying for it that is fair and equitable. And we proposed a surtax at that time, a surtax before loopholes and before accelerated depreciation or investment tax credits on individuals and corporations by an amount equal to the extent of the defense increase.

If we had done that, if that had been done—and I think not doing it was a deeply damaging thing—we wouldn't be facing the deficit problem that we are facing today and have this poison pill in the system that is going to suffocate, some of the things that are going to have to be done years ahead, long into the future.

The **Chairman**. Senator Moynihan.

Senator **Moynihan**. Mr. Chairman, could I comment on just that point. The problem was that we were, at least in part, dealing with an administration that was not so much divided but rather had two purposes: It wanted simultaneously to increase one part of the budget while decreasing another. It used the strategy of an induced deficit to make the case for decreasing the social side, never thinking that anybody would ever say, "But what about this other part of the same budget which ends up in the same deficit?" This is what is happening now, just exactly what you said.

The increase in defense spending which began under President Ford in his last budget, has come under such a general cloud, "We can't afford it; therefore, we won't do it." And as you always said we can afford whatever we need, but we have to pay for it.

Let me read to you from this journal, "Profile," in Vienna, March 25, 1985. It is Frederich von Hyack, saying, that the President explained to him that unless you piled up debts that were so huge it would not be absolutely clear to everyone that no additional money could be spent. In this way he was hoping to convince Congress, by means of an enormous deficit, of the necessity of a reduction in expenditures. Unfortunately, he didn't succeed; but, nevertheless, this explanation makes it understandable why a sensible man could do such a thing.

Then he goes on to talk about just this point. Now the defense strategies are in danger, too. They created a deficit designed to undo Social Security, and they are going to end up undoing their 400-ship Navy, don't you think?

Mr. KIRKLAND. Yes.

Senator MOYNIHAN. If you thought, Mr. Kirkland, that this tax proposal before us was going to add another $100 or $200 billion to the deficit in the next 5 years, would you be for it?

Mr. KIRKLAND. No.

Senator MOYNIHAN. No. Would you think it would jeopardize still further that Defense Program you were concerned about?

Mr. KIRKLAND. Yes.

Senator MOYNIHAN. Yes. And if the Joint Committee on Taxation this week issues a report that says something like this is possible—you have mentioned that the CBO and others have made such estimates—we could be sitting here on another tax bill, couldn't we? And that deficit just goes on forever. And it begins not just to beat down the social programs but it starts to beat down the Defense Program, too, doesn't it?

Mr. KIRKLAND. No question, sir.

I would be delighted to provide the committee with the rather detailed alternative budget and tax proposals that we prepared in 1981, 1982, 1983, and so forth, and each of them would have achieved a significant reduction in the deficit.

Senator MOYNIHAN. Would you do that?

Mr. KIRKLAND. Yes.

Senator MOYNIHAN. I think this committee should have that, and I thank you.

[The proposals follow:]

1984

Background Paper on The National Economy

The Administration proposes to increase defense outlays in 1985 to $272 billion, an increase of 15 percent.

This Council has called for reducing real defense spending increases to a range of 5 to 7 percent, with some members urging that the increase be held to the lower end of the range or below.

Savings from this lowered defense spending would be $7 to $12 billion in the first year, with substantially greater reductions in future years, assuming an inflation rate of 5 percent.

To pay for real increases in defense spending, we have supported a progressive surtax levied on corporate and individual income taxes, plus an additional tax on income currently sheltered. Such a surtax would raise $12 billion to $17 billion in the first year.

A number of the programs that the AFL-CIO calls for would provide for increased expenditures. But to the extent that people are put back to work under these programs, they would become taxpayers rather than recipients of unemployment compensation or in some cases welfare benefits. Each one-percent reduction of unemployment raises tax revenues by about $25 billion and reduces outlays by $5 billion.

Following are the budget estimates for the detailed programs spelled out in the AFL-CIO recommendations:

The Industrial Policy Act (H.R. 4360) would set up a new process for dealing with industrial economic issues through a new Council on Industrial Competitiveness, whose cost would be small. The Bank for Industrial Competitiveness would have a federal authorization for $8.5 billion in federal stock subscription made available over several years.

The Community Service Jobs Act (H.R. 1036 and S. 1812) calls for an authorization of $3.5 billion to employ people in community service work who cannot find jobs in the private sector .

The Public Works Act (H.R. 2544) would carry an authorization of $3.2 billion to help reconstruct the nation's basic infrastructure, including water and sewer facilities, highways and port facilities, and other public works which stimulate private, job-creating investment and economic activity.

The Plant Closing Act (H.R. 2847) would have little budget impact; it would require employers to provide advance notice and some basic protections for workers and local communities.

The domestic auto content bill (H.R. 1234 and S. 707) would have no measurable budget outlays but would assure continued extensive U.S.auto production.

The Health Care Protection Bill (H.R. 3521) calls for authorization of $1.8 billion a year for each of two years to provide health insurance coverage for the unemployed.

The health care cost containment legislation would save the federal government $1 billion. We oppose the President's call for cuts of $1.1 billion in Medicare and $1.1 billion in Medicaid.

The energy bills, women's pension and insurance protections, consumer and worker protections in telephone, and consumer and worker protections in bankruptcy have little budget impact, but provide substantial worker and consumer safeguards.

We are opposed to the President's call for cuts of $200 million in authorization for elementary, secondary and vocational education and for cuts of $900 million in higher education loans and grants.

We are opposed to the President's call for cuts of $600 million in employment and training programs.

There is a saving to the government in our proposals for improving the single-employer pension guarantee program.

In addition, the AFL-CIO has proposed a second rollback of the personal and corporate income tax reductions enacted in 1981, and the closing of some earlier corporate tax loopholes, which would add up to an estimated $49 billion in additional tax revenues in fiscal year 1985.

This is just a partial recapture of the $165 billion in revenue loss that occurs in 1985 as a result of the 1981 Tax Act. Congress made a start in 1982 to correct this revenue shortfall problem.

Additional Federal Revenues From AFL-CIO Tax Proposals

	Fiscal Year 1985 in Billions
$700 Cap -- Third Year	$ 6.9
Repeal Indexing	6.2
Trim "Savings" Exclusions	2.7
Phase Down Capital Gains	3.9
Scale Back Estate and Gift Exclusion	3.7
Foreign Tax:	
DISC	1.4
Deferral	1.0
Foreign Tax Credit	7.1
Investment Tax Credit:	
Depreciation Basis Adjustment	1.3
Reduce 10% to 7%	7.1
Limit Graduate Rates to Small Corporations	2.0
Oil and Gas Depletion & Expensing of Drilling Costs	6.0
	$49.3

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ATTACHMENT A

1983

AFL-CIO ECONOMIC PROGRAM FOR JOBS AND FAIRNESS

ATTACHMENT B

BILLIONS OF DOLLARS

This table details the deficit reductions possible through the AFL-CIO program. The combination of tax measures and defense savings over the 1984-1986 period add up to over $300 billion and most of these savings would continue in later years. The cost of programs to create jobs, help the unemployed and restore fairness add up to essentially a one time increase in expenditure of $87.8 billion. Deficits would also be reduced as employment gains create additional incomes and tax revenues.

INCREASED REVENUES & SAVINGS

	Fiscal Year (Billions)		
Taxes	1984	1985	1986
$700 Cap—third year	$ 6.0	$ 6.9	$ 7.4
Repeal Indexing	0.0	0.9	23.4
Trim "Savings" Exclusions	0.6	1.7	3.7
Phase Down Capital Gains Exclusions	2.5	5.6	8.1
Scale Back Estate & Gift Tax Exclusions	1.6	2.1	2.0
Foreign Tax:			
DISC	2.0	3.0	3.0
Deferral	6.0	6.6	7.1
Foreign Tax Credit	6.5	7.1	7.4
Investment Tax Credit:			
Depreciation Basis Adjustment	1.3	2.4	4.1
Reduce 10% to 7%	5.6	7.1	8.2
Limit Graduated Rates to Small Corporations	1.9	2.0	2.0
Oil & Gas Depletion & Expensing of Drilling Costs	7.2	8.0	9.0
	$41.2	$61.4	$86.2
Defense:			
5-7% Surcharge	$11-$15	$23-$32	$37-$52
Lower (5-7%) Real growth	5-3(14)	17-7(31)	25-13(33)
Total Taxes & Savings	$57-$59	$101-$100	$148-$151

INCREASED BUDGET OUTLAYS

Jobs & Recession Relief	Supplement to FY 1983 (Billions)	1984	Direct Jobs (thousands) 1983	1984
Comm. Development Supplemental Jobs	$ 5.0	$10.0	420	835
Youth Programs	1.5	3.0	215	430
Displaced Worker Program	1.0	2.0	—	—
Housing	5.0	10.0	85	100
Accelerated Public Works	5.0	10.0	170	340
Extended Unemployment Insurance	2.0	6.0	—	—
Health Care for the Unemployed	3.0	5.0	—	—
	$22.5	$40.0	890	1,765
Rescind Proposed Budget Cuts in Non Defense		19.3		
TOTAL INCREASED OUTLAYS	$22.5	$65.3		

*[illegible] July 1981 [illegible] 5%-7% real growth.

**[illegible]

Additional Federal Revenues
From AFL-CIO Tax Proposals

	Fiscal Year 1985 in Billions
$700 Cap—Third Year	$ 6.9
Repeal Indexing	6.2
Trim "Savings" Exclusions	2.7
Phase Down Capital Gains	3.9
Scale Back Estate and Gift Exclusion	3.7
Foreign Tax:	
DISC	1.4
Deferral	1.0
Foreign Tax Credit	7.1
Investment Tax Credit:	
Depreciation Basis Adjustment	1.3
Reduce 10% to 7%	7.1
Limit Graduate Rates to Small Corporations	2.0
Oil and Gas Depletion and Expensing of Drilling Costs	6.0
	$49.3

1982

Fact Sheet

An Alternative to Reaganomics

The Alternative provides for: increase revenues from undoing the worst aspects of last year's tax giveaways, scrutinizing defense outlays and financing any required increases with a corporate and individual surtax, restoration of newly proposed budget cuts, and establishing new jobs programs. It points out ways to raise additional revenues by closing specific tax loopholes:

INCREASE REVENUES

Increased Revenues from Revisions of Tax Law

	Anticipated Revenues (in billions)	
Cap the 1982 and 1983 individual tax cuts at $700 per family	$20	
Repeal the leasing of tax credits by corporations	8	
Repeal the new loopholes in the oil windfall profits tax	2	
Modify the widened estate and gift tax provisions	1	
Repeal the future indexing of tax rates	—	
Total	$31 billion	
Increased Revenues from Savings		
Scrutinize defense outlays and finance any required increases with a corporate and individual surtax		
Current proposed defense budget increase	$33	
Total	$33 billion	
Total of Increased Revenue & Savings		**$64 billion**

ATTACHMENT C

NECESSARY OUTLAYS

New Jobs Programs

	Anticipated Expenditures (in billions)
Invest in public infrastructure for the nation's deteriorating communities, including sewer, highway, bridge, mass transit, railroad, and other needed facilities	$ 5
Invest in human capital through effective training of the unemployed and provide public employment opportunities for those who still cannot find work after lengthy searches	5
Encourage low- and moderate-income housing	5
Establish a Reconstruction Finance Corporation to rebuild the nation's industrial base by aiding sectors of the economy and of the country that need special assistance through loans, grants or guarantees	4
Limit harmful imports that aggravate the impact of the recession and weaken key industries	—
Extend unemployment insurance benefits to protect the long-term jobless	4
Total	$23 billion
Restore Budget Cuts	
Restore Proposed Budget Cuts	41
Total	$41 billion

Total New Jobs & Restoring Budget Cuts $64 billion

The Chairman. Senator Mitchell.

Senator Mitchell. Thank you, Mr. Chairman.

Mr. Kirkland, at pages 6 and 7 of your statement you recommend a number of proposals which may be characterized as codifying some of the benefits that the President's tax plan provides for business. The argument for these and other similar proposals has been made before this committee by the administration and by business leaders. The argument is that such proposals are necessary to ensure the formation of capital and the investment and reinvestment in business, which of course is what creates jobs.

What is your response to that? What do you say to someone who makes that argument? You represent working men and women; you are obviously interested in healthy economic development, the creation of new jobs, the maintenance of existing jobs. How do you respond to that argument?

Mr. Kirkland. Senator Mitchell, over the years I have heard that argument. An awful lot of sins are committed or proposed in the name of capital formation, and it is common argument in dealing with the human objective of easing one's tax burden as much as possible, and keeping the money to the maximum extent possible, which I think is a fairly universal aspiration. But I have asked businessmen, in their relaxed moments at times, "What is the single factor that most affects your decision to invest your money into the production of a product? Is it taxes? Is it location? Is it concessions from the State?" And after a lot of discussion, almost invariably the answer I ultimately get is, "Can I sell the damn thing?" If you can't sell the damn thing, all the tax breaks in the world are not going to make that a prudent decision. And the market? That's what the market means, is there a market for the product? Is the product good? Does it have that kind of appeal? I think that still is the driving force behind investment decisions, and I think it ought to be.

You know, over the years, for some years now, we have had a labor-management group that meets informally from time to time. It had its inception as the President's Labor-Management Advisory Committee. It subsequently ceased business in that form and resumed its meeting on a private, unofficial basis. But at the time, and as I recall it was in the Ford administration, that committee was asked to give its recommendations on a tax package. We had intensive discussons, and it involved a tax cut. We reached agreement on what was the appropriate distribution of that tax, and the same consideration would have applied in the case of a tax increase, as between individuals and appropriations, what was their appropriate share of that burden or reward. And we reached a unanimous agreement that the appropriate division was 75 percent individuals, 25 percent corporations.

We jointly approached the Ways and Means Committee on that basis, on the basis of the plan we worked out at that time, labor and management. And that 25 percent has sort of withered away, along with a lot of other things; but I still think it is probably a pretty good rule of thumb, rough and ready breakdown. There was a point when that was the effective contribution of individuals and corporations to the revenue base. We have gotten a long way from it.

Senator **Mitchell**. I see that my time is just about up, so I thank you, Mr. Chairman.

Thank you, Mr. Kirkland.

The **Chairman**. Senator Chafee.

Senator **Chafee**. Thank you very much, Mr. Chairman. I apologize that I was at an Environment and Public Works hearing and could not be here earlier. So some of the questions I ask may be redundant.

What percentage of your members would you think itemize so they take advantage of the local real estate and State tax deductions? Do you have any idea?

Mr. **Kirkland**. I am advised by my technical expert that it is probably between 40 and 50 percent.

Senator **Chafee**. Oh, that high? Forty or fifty percent would itemize?

Let me ask another question. On the corporate tax rate, how high do you think it ought to be?

Mr. **Kirkland**. I would say high enough to achieve a 75-to-25 contribution to revenue times what the revenue needs of the country are.

Senator **Chafee**. Do you mean vis-a-vis the individual?

Mr. **Kirkland**. Yes.

Senator **Chafee**. Seventy-five percent from individuals, 25 percent from corporations, and take what you need.

Mr. **Kirkland**. Or how far you are willing to go torward raising the revenue that the country requires.

Senator **Chafee**. In other words, have it at a consistent 25 percent.

We have had a lot of testimony in here in the previous days on the corporate rate, the ITC, investment tax credit, all relating to jobs. What do you think about all that? What do you think about the relationship of the corporate tax on the ability of American industry to produce jobs?

Mr. **Kirkland**. I don't think it is irrelevant, sir. I think it is one of the tools that ought to be available in addressing the specific problems of specific industries. We have long been supporters of an approach that travels in discussions under the label of "industrial policy," and we have argued that those tools ought to be available on a targeted basis, that that largesse, if it is going to be offered, should not fall upon the washed and the unwashed alike, but that it ought to be reserved as part of a set of tools to achieve certain objectives on a sectoral basis.

Senator **Chafee**. Are you talking about the investment tax credit now?

Mr. **Kirkland**. I am talking about the investment tax credit and accelerated depreciation, all other of those tolls. And the conditions ought to be negotiated, I think, under the broad framework of an industrial policy. I think if a company tells you in an abstract way that an investment tax credit is going to produce large-scale improvements in jobs, I think you ought to have some commitments from the companies as to just what they are going to do with that money, and have them stand and deliver.

Senator **Chafee**. So, you would have us repeal it except in certain instances?

Mr. KIRKLAND. I believe those tools ought to be available on a selective, targeted basis as part of a general industrial policy approach.

Senator CHAFEE. Who would determine who gets it? Us, the Finance Committee?

Mr. KIRKLAND. No; I do not believe the Finance Committee should determine who gets it. I think there ought to be a formal—in fact, I would recall that during the last couple of years of the Carter administration we worked out with the administration something called the national accord, on the basis of which we voluntarily agreed to take part in a system of wage restraints.

There was at that time a wage policy committee formed on a tripartite basis. We participated in it after having neogitiated with the administration this national accord, and the national accord had other features. One of them was the creation of a National Reindustrialization Board, on a tripartite basis. And that National Reindustrialization Board would be charged with the task of developing and proposing policies to the Congress and to the administration, seeking the authority to do the things that it might find desirable to achieve the objective of reinvigorating and reviving our industrial capacity, which I see and saw then and still see as gravely threatened in this country.

A part of the charge of that Board was to propose a mechanism for a financial entity somewhat along the lines of the old RFC, and to be a forum whereby industries that sought relief or help, as a number of them have, as this Government has had to move in on an ad hoc basis and deal with—Chrysler, Lockheed, Continental Illinois, a slew of them on an ad hoc basis—that this be the forum and the channel through which those appeals were made, and that an understanding in those cases be negotiated with the parties in question, and that various tools would be available, including these tax abatement devices, on consideraton of assurances from the other side, from the beneficiary.

I still believe that is the soundest approach when you are dispensing these special breaks, and I know it has been discussed and I presume is still under discussion in different committees and subcommittees of the Congress, and there have been various proposals of that sort offered. But nothing yet has been done. We believe it should be.

Senator CHAFEE. Thank you. I notice my time is up.

Thank you, Mr. Chairman.

The CHAIRMAN. I have no questions. Senator Moynihan?

Senator MOYNIHAN. No questions, Mr. Chairman.

The CHAIRMAN. Senator Mitchell?

Senator MITCHELL. No more questions, Mr. Chairman.

The CHAIRMAN. Do you have any more, Senator Chafee?

Senator CHAFEE. No more, Mr. Chairman.

The CHAIRMAN. Mr. Kirkland, thank you very much.

Mr. KIRKLAND. Thank you.

The CHAIRMAN. Now we will have a panel consisting of Dick Warden representing the United Automobile Workers; Richard Cordtz, the international secretary-treasurer of the Service Employees Union; and Eddie Carlough, the general president of the Sheet Metal Workers.

Mr. Warden, why don't you go right ahead?

STATEMENT BY DICK WARDEN, LEGISLATIVE DIRECTOR, INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE AGRICULTURAL IMPLEMENT WORKERS OF AMERICA, WASHINGTON, DC, ACCOMPANIED BY ALAN REUTHER, ASSOCIATE GENERAL COUNSEL, AND LYDIA FISHER, UAW ECONOMIST

Mr. WARDEN. Mr. Chairman, my name is Dick Warden. I am the legislative director of the UAW, and I am accompanied this morning by UAW associate general counsel Alan Reuther to my left, and UAW economist Lydia Fisher. We appreciate very much the opportunity to be here. We will attempt to avoid repetition of President Kirkland's statement. Much of what is contained in our statement you have already heard. Instead we will ask that our full statement be included as part of the hearing record and go ahead and summarize it.

The CHAIRMAN. All of the statements will be in the hearing record in full. And as you noted, Mr. Kirkland confined his statement to 5 minutes, and we would appreciate it if you could all do the same.

Mr. WARDEN. I will try very hard, Mr. Chairman.

The UAW represents 1.5 million active and retired members and their families. We have for years advocated reforms to make the Tax Code more equitable and progressive, and we believe that the interest expressed by Members of Congress on both sides of the aisle and by the President represents a positive development which could lead to great improvement in the fairness of the Tax Code.

Although certain aspects of the President's proposal do have considerable merit, we also believe that the plan contains a number of objectionable provisions from our standpoint, and our statement goes on to refer to a number of those concerns.

For one thing, President Reagan has described his tax reform plan as revenue neutral, but the Treasury Department's own estimates and those of the CBO show that from 1986 to 1990 the plan would yield less revenue than current law. We have all read in recent days about the report that is due from the Joint Tax Committee. But worse yet, greater losses have been predicted by other economists who have looked at this and made projections. In fact, the Treasury's estimates are based on economic forecasts that are much more optomistic than the consensus of most private economists.

The UAW believes the enactment of tax proposals resulting in a loss of revenue would be unconscionable in light of the current serious budgetary problems facing the country. So we urge that this committee guard against any weakening of the Federal Government's revenue base. We hope the committee will insist, at a minimum, that any tax reform plan that it reports will be truly revenue neutral.

Because we are so concerned about the ability of our tax system to raise sufficient revenues to finance the needed services of government, I will go ahead and anticipate a possible question and say that if the committee does decide to opt for a bill which would increase taxes, we would support it and support it enthusiastically, provided that working and poor Americans are not fairly burdened and that corporations and wealthy individuals pay their fair share.

The President's recommendations would virtually eliminate Federal income taxes for families at or below the poverty line. We have long supported those kinds of proposals designed to take the poor off the tax roles. We are particularly pleased that the President's plan would increase and index the earned-income tax credits, steps which are efficient and direct in reducing taxation of the poor.

We are concerned, however, that the President's proposals are unfairly tilted toward the wealthy. As a group, taxpayers in the $20,000 to $50,000 income bracket would receive an average tax cut of 7.6 percent, while those at $200,000 and over would get 10.7 percent.

Since the Reagan administration took office, the tax burden on wealthy persons has declined sharply. The 1981 tax legislation slashed the top rate of the wealthy from 70 percent to 50 percent; now the President proposes another reduction to just 35 percent, exactly half of where the top rate was prior to 1981. We would support the addition of higher tax rates, above those proposed in the President's plan for the wealthy. This would help raise additional revenue and would make the tax reform package more fair and progressive.

The UAW continues to strongly oppose any proposals to impose Federal income and Social Security taxes on employer-provided health insurance benefits. Our statement goes into considerable detail on this point and addresses some of the questions raised earlier by Senator Mitchell. Regardless of whether the tax is structured along the lines of a floor, as in the Presidential package, or as a cap as in Treasury One, we believe that once any portion of employer-provided health care benefits is taxed that complete taxation of such benefits will soon follow. The Federal Government's continuing need for additional revenues will inexorably create pressure to raise the tax floor or to lower a tax cap, we believe.

We therefore urge the committee to reject any package of taxes which includes taxes on health care benefits received by workers and their families. As I say, our prepared statement goes into considerable detail on this point.

The UAW is pleased that the President's plan would retain the tax treatment of employer-provided life insurance and childcare benefits. We are also pleased that the package would make permanent the tax-exempt status of employer-provided educational assistance and group legal sevice benefits.

We would like to take this opportunity to commend the chairman, particularly, of this committee for his consistent leadership in defending the tax-exempt status of employee benefits.

The UAW does not believe the President's proposal to increase the limits on tax-deductible contributions to spousal IRAs, as they are called, is justifiable at this time, given our revenue situation.

The **Chairman**. I am going to have to ask you to conclude, Mr. Warden.

Mr. **Warden**. Yes, sir.

We appreciate very much, Mr. Chairman, the opportunity to have been here this morning. Our statement goes on to mention a number of other points, including our opposition ot the elimination of the deductibility of State and local taxes, and other points that we have made in our prepared statement.

I would say in conclusion, Mr. Chairman, that the UAW appreciates very much the opportunity to have been here this morning to share our views on the President's tax reform proposal with you. Thank you.

[Mr. Warden's prepared testimony follows:]

July 24, 1985

Statement of

Dick Warden, Legislative Director
International Union, UAW

on the subject of

President Reagan's Proposal for
Comprehensive Tax Reform

before the

Committee on Finance

of the

United States Senate

On behalf of:

International Union, United Automobile,
Aerospace & Agricultural Implement
Workers of America, (UAW)

Mr. Chairman, my name is Dick Warden. I am the Legislative Director of the United Automobile, Aerospace and Agricultural Implement Workers of America (UAW). I am accompanied this morning by UAW Associate General Counsel Alan Reuther and UAW Economist Lydia Fischer. We appreciate the opportunity to be with you to share the views of the UAW with respect to President Reagan's proposals for tax reform.

The UAW represents 1.5 million active and retired members and their families. Our Union has long been an advocate of reforms to make our tax code more equitable and progressive. To that end, we have consistently supported measures designed to assure that working men and women are treated fairly under our system of taxation, that the poor are not taxed, and that wealthy corporations and individuals pay their fair share of taxes. We have been guided in our actions by the principle of "ability to pay" which, we believe, is a fair way to evaluate the proper impact of the tax code on individuals and corporations. The UAW believes the interest expressed in tax reform by the President and by Members of Congress on both sides of the aisle represents a positive development which could lead to great improvement in the fairness of our tax code.

At the same time, we must also be on guard against misuse of the slogan "tax reform" to advance other, more questionable ends. "Tax reform" must not become a Trojan horse for further depriving the federal government of an adequate level of revenues to fund vitally necessary services and programs. Nor should it result in further needless giveaways to our nation's wealthiest taxpayers who have already benefited so enormously from the major tax revisions enacted in 1981. Nor should "tax reform" become a vehicle for shredding American workers' health care, unemployment and workers compensation safety nets; for making it even more difficult for cities and states to raise needed revenues and to provide adequate services; or for eroding support for public and private pension systems. Although certain aspects of the President's tax reform proposal do have some merit, it is the UAW's considered opinion that the President's plan also contains many objectionable provisions.

"Revenue Neutrality"

President Reagan has described his tax proposals as "revenue neutral". But the Treasury Department's own estimates and those of the Congressional Budget Office (CBO) show that from 1986 to 1990, the plan would yield less revenue than current law. Worse yet, CBO and others predict greater losses beyond 1990. Moreover, the Treasury's estimates are based on economic forecasts that are much more optimistic than the consensus of private economists. An economic downturn would most certainly exacerbate the revenue shortfall produced by the President's proposals.

The UAW believes the enactment of any tax proposals which would result in a loss of additional revenue to the federal government would be unconscionable in light of the serious budgetary problem facing the country. Due in large part to the Reagan Administration's ill-advised and misdirected 1981 tax cuts, and to massive increases in military spending under this Administration, the federal government has been running deficits of unprecedented size during a period of economic expansion. And despite the deep, unwise cutbacks in essential social programs instituted under the Reagan Administration, large federal deficits are projected to continue for the rest of the decade. Accordingly, the UAW strongly urges this Committee to guard against any further weakening of the federal government's revenue base. We urge the Committee to insist at a minimum that any tax reform plan be truly "revenue neutral" — and not simply a disguised tax cut.

Because we in the UAW are concerned about the ability of our tax system to raise sufficient revenue to pay for functions our society has wisely entrusted to the federal government, the UAW would be willing to support a tax reform package that actually raises additional revenue, provided that working and poor Americans are not unfairly burdened and that corporations and wealthy individuals pay their fair share. We recognize, however, that the Members of this Committee may currently feel constrained by President Reagan's announced opposition to any revenue raising initiatives. But if the President or this Committee should subsequently decide that such initiatives are necessary, the UAW is prepared to work with the Members of this Committee in fashioning equitable measures which would raise additional revenue to help attack the deficit problem facing this country, and to insure that our government has sufficient revenue to finance urgently needed social programs.

Taxation of the Poor

The President's recommendations would virtually eliminate federal income taxes for families at or below the poverty line. As stated earlier, we have long been on record in support of tax reforms designed to take the poor off the tax rolls. As a matter of simple equity, and as a means of attacking poverty, the UAW believes that any tax reform legislation should eliminate taxation of the poor, whose ranks have grown substantially as a result, we believe, of cutbacks in social programs and other policies of this Administration. We are particularly pleased that the President's plan would increase and index the earned income tax credit — steps which are most efficient and direct in reducing taxation of the poor.

Progressivity of the Tax Code

The UAW is extremely concerned that the President's proposals are unfairly tilted towards the wealthy. As a group, taxpayers in the $20,000 to $50,000 income bracket would get an average tax cut of 7.6 percent, while those at $200,000 and over would get a 10.7 percent tax cut. The reduction in tax rates for the wealthy would give them, once again, exorbitant and unnecessary tax windfalls. For example, the

President's proposal would result in a tax cut of about $60,000 (or 23 percent) for many families in the $600,000 income level.

Since the Reagan Administration took office, the tax burden on wealthy persons has declined sharply. The 1981 tax legislation slashed the top tax rate of the wealthy from 70 percent to 50 percent. Now the President proposes another reduction to just 35 percent — exactly half of where the top rate stood prior to 1981. Moreover, this proposal would shower additional benefits on the wealthiest segment of society because it translates into an even more liberal tax treatment for capital gains — long a sore point among workers whose income is derived mostly from wages.

The UAW submits that there is no justification for providing further tax benefits to the wealthy. That can only serve to reinforce the public's deep-seated feeling that the tax code is basically unfair and skewed to the advantage of the wealthy.

The UAW strongly supports the addition of higher tax rates for the wealthy. This would help to raise additional revenues, and would make the tax reform package fairer and more progressive.

Taxation of Health Insurance Benefits

The UAW continues to be strongly opposed to any proposals to impose federal income and Social Security taxes on employer-provided health insurance benefits. The President's plan calls for a tax "floor" on health care benefits, by taxing the first $25 a month of employer-provided health insurance benefits for an employee with a family, and the first $10 a month for single employees (for a total of $300 and $120 a year respectively). The proposal contained in the Treasury Department's original plan would have imposed a "cap" on the amount of tax exempt employer-provided health insurance benefits at $175 a month for worker with a family, and $70 a month for a single worker. In our judgment, both proposals are unacceptable. Regardless of whether the tax is structured along the lines of a "floor" or a "cap", once any portion of employer-provided health care benefits is taxed we believe that complete taxation of such benefits will soon follow. The federal government's continuing need for additional revenues will inexorably create pressure to raise a tax "floor" or to lower a tax "cap" (just as has occurred with respect to the taxation of unemployment compensation benefits). We therefore urge Congress to reject any package that taxes any portion of the health care benefits received by workers and their families.

Today more than 90 percent of full-time workers are enrolled in employer sponsored group health care plans. The growth of group health insurance coverage among workers and their dependents has promoted wide access to health care. This has contributed to the financial security and peace of mind of Americans, as well as the remarkable improvement in their health and longevity. The preservation of this network of protections is vitally important, particularly in view of our nation's failure to adopt a universal national health care program.

The UAW is convinced that the taxation of employer-provided health insurance benefits would seriously jeopardize this network of protections. The imposition of federal income and Social Security taxes on health care benefits would have a detrimental impact on the distribution and availability of these benefits among the workforce. In the case of non-cash fringe benefits, such as health insurance, where the fringes are provided in the form of in-kind services and cannot be converted to cash under any circumstances, the imposition of federal income or payroll taxes will inevitably have a chilling effect on the commitment of employers and employees to the growth and development of these benefits. The additional costs and administrative burdens will dampen the enthusiasm of employers. And employees are likely to find the taxation of these benefits to be unacceptable, because there would be an increase in their tax burden while nothing is added to their earnings, resulting in a net reduction in their take-home pay.

Moreover, the imposition of federal income and Social Security taxes on health insurance benefits would constitute a tax increase that would fall most heavily on low and middle income workers. Regardless of how the tax is structured, taxing health care benefits would make our tax system less progressive and therefore less fair — just the opposite of the President's purported objective. Indeed, as currently structured, the tax "floor" on health care benefits would surely put some of the working poor back on the tax rolls.

The Treasury Department's original proposal to impose a "cap" on the amount of tax free health care benefits is also fatally flawed. It would threaten the integrity of existing health insurance plans and would adversely affect beneficiaries because:

- It would create pressure to reduce negotiated health care benefits, to add copays and deductibles, and to drop various coverages (such as dental and vision care) from employee health benefit plans.
- It would penalize groups with more older workers who need to use more health care service. This in turn would discourage employment of older workers.
- It would act as an incentive for the younger, healthier workers to leave health plans, opting instead for reduced, inadequate coverage, and raising the cost of the plans for remaining workers. The fragmentation of plans would add to the administrative costs of employers.
- It would penalize workers in higher risk occupations, such as assembly line workers, steel and foundry workers, and mineworkers.
- It would unfairly affect certain geographic regions because of variations in medical care costs in different areas.

- It would put pressure on employers and unions to reduce coverage for preventive health services. Such barriers to prevention and early treatment of illness could lead to increased use of high cost hospital inpatient facilities.

The taxation of health care benefits would not be effective in stemming the rapid rise in health care costs. Inflation in the health care sector is not due to too little cost sharing among workers. Most workers covered by health insurance are still exposed to substantial out-of-pocket payments for personal health services. Inflation in the health care industry also cannot be attributed to the expansion of health insurance coverage. In fact, health insurance coverage practically ceased growing in the 1970s, while that period and the early 1980s have seen the greatest increases in health care costs along with increases in consumer out-of-pocket payments.

A careful examination of the problem suggests that health care inflation has multiple causes including cost-based reimbursement of hospitals, reimbursement of physicians on a fee-for-service basis, provider generated overuse of services, the introduction and spread of expensive high-tech equipment, aging of the population, excess hospital capacity and the absence of any rational comprehensive cost control program. Taxing health care benefits will not attack these root causes of inflation.

Tax Treatment of Retirement Savings and Other Employee Benefits

The UAW is pleased that the President's plan would retain the existing tax treatment of employer-provided life insurance and child care benefits. We are also pleased that the tax reform package would make permanent the tax-exempt status of employer-provided educational assistance and group legal services benefits. The UAW commends the Chairman of this Committee for his consistent leadership in defending the tax-exempt status of these employee benefits. They address vital needs and provide valuable assistance to workers and their families, which in turn benefits society as a whole. For example, employer-provided educational benefits have played an important role in alleviating worker dislocation and unemployment therefore reducing the costs of both to the rest of society.

The UAW also commends the President for proposing new non-discrimination rules, which would be applicable to all tax favored employee benefits. We firmly believe that the favorable tax treatment accorded various employee benefits should be made contingent on strict non-discrimination rules. There is no justification for permitting professional corporations or upper income individuals to use various fringe benefits as a device for sheltering earnings.

We urge Congress to reject the President's proposal to eliminate the $5,000 exclusion for death benefits. This proposal would raise negligible amounts of revenue, yet would have an unnecessarily harsh impact on the spouses and dependents of deceased workers.

The proposal to allow expiration of the tax credit for employer contributions to an ESOP also seems to us to be unwise. This tax credit helps to promote employee ownership of their employer's stock.

The President's plan contains a number of positive proposals relating to the tax treatment of retirement savings. In particular, the proposals to apply uniform distribution rules to all types of retirement savings plans, to simplify the rules governing the limits on pension contributions and benefits, and to insure that funds contributed to retirement plans are actually used for retirement purposes by imposing a stiff excise tax on premature distributions, are all positive steps. In addition, the UAW supports various reforms that have been proposed by the President with respect to 401(k) plans, including lowering to $8,000 the limit on discretionary employee contributions, tightening the distribution rules which are applicable to these plans to encourage the retention of monies for retirement purposes, and offsetting the allowable contributions to IRAs and 401(k) plans. The UAW also strongly supports the proposals to repeal 10 year income averaging and capital gains treatment for lump sum distributions.

We are concerned, however, that the President's plan also contains proposals with respect to retirement savings that could have an adverse impact on the continued growth and development of retirement plans. For example, although we support the principle underlying the proposed rules relating to the imposition of an excise tax on premature distributions from retirement plans, we believe that the rules should be structured in a manner that will not interfere with the operation of bona fide early retirement programs. Similarly, the proposal to place an excise tax on the reversion of excess assets to employers upon the termination of a defined benefit pension plan could have a deleterious impact on the funding of such plans, without providing any meaningful remedy for the numerous abuses which have arisen in connection with termination-reversions. We also believe that the 401(k) reforms should make it clear that tax exempt organizations can make these types of plans available to their employees.

The UAW is strongly opposed to the President's proposal to increase the limits on tax deductible contributions to "spousal IRAs" from $250 to $2,000. Although the Administration has touted this proposal as being a "pro-family" measure which will help homemakers, in fact the proposal will contribute little or nothing to the retirement income security of most homemakers.

The available data clearly demonstrates that the wealthy receive a disproportionate share of the tax benefits associated with IRAs. Raising the limit on tax deductible contributions to spousal IRAs will simply aggravate this situation since, for the most part, only higher-income families will have sufficient disposable income to be able to contribute the extra $1,750 to a spousal IRA. We are also concerned that, in the long run, the continued expansion of IRAs will wind up undermining public support for Social Security and the private pension system, which in our judgment represent the best means of providing adequate retirement income security to working men and women and their spouses. Instead of expanding IRAs, as the President has proposed, we would recommend that the existing IRA limits be retained, and that the deduction for IRA contributions be converted to a credit, to make it more equitable for middle and lower income workers.

Taxation of Unemployment and Worker Compensation Benefits

The UAW is strongly opposed to the President's proposals to tax unemployment and worker compensation benefits. One of the rationales advanced by the Reagan Administration to support these proposals is that providing tax free income to people who are unemployed or disabled will keep them from seriously looking for work or from getting back to their jobs. We reject this argument, which seems to assume that unemployment and disability are conditions enjoyed by workers, rather than misfortunes visited upon them.

In determining what level of benefits is needed under their unemployment and worker compensation programs in order to provide persons with an adequate income, the states have been cognizant of the fact that these benefits are for the most part tax free. If the President's proposals to tax these benefits were to be enacted, however, we doubt that the states would promptly adjust their benefit levels. The more likely result is that unemployed and disabled workers would simply wind up with their income being reduced. As a result, these proposals would partly offset the tax relief for the working poor and the near-poor provided elsewhere in the tax reform package.

The UAW also notes that the President's proposal continues the exclusion from taxation of disability benefits provided under veterans' programs (in contrast to the original Treasury proposal, which taxed them fully). There is no justification for treating such benefits differently from worker compensation or black lung disability benefits. We therefore urge this Committee to adopt a uniform approach which exempts all disability payments from taxation.

Deductibility of State and Local Taxes

The UAW is flatly opposed to the President's proposal to repeal the deduction for state and local taxes. This proposal would severely impair the ability of states and cities to meet their own fiscal needs. It would pressure states and cities to reduce their taxes, to offset the effect of the elimination of deductibility on taxpayers' total tax bills, and to prevent the flight of taxpayers to low tax areas. Thus, the President's stated goal of revenue "neutrality" obviously would not extend to states and cities.

As a result of this reduction in their revenue base, states and cities would in turn be forced to curtail essential social services. Educational programs would especially suffer, since they make up the single largest item in state budgets. Study after study has shown that our society needs to step up its efforts in the educational arena. Yet disallowing deductions for state and local taxes would seriously undermine public acceptance of the state and local revenue mechanisms which support education, and would inevitably lead to a decline in educational standards along with other human services.

The President's proposal represents a "double whammy" for states, especially the most industrialized and populous ones where the majority of UAW members live. As a result of this Administration's efforts, the federal government has already required states to shoulder more responsibility for social programs by reducing or eliminating federal assistance. The proposal to disallow the deductibility of state and local taxes would make it harder for states and cities to raise the revenues needed to meet these responsibilities. We therefore urge this Committee to reject this proposal.

Other Individual Income Tax Provisions

The UAW opposes eliminating the second-earner deduction. That provision was put into effect in recognition of the increasing number of two-earner families, and the "marriage penalty" that resulted from having two earners with comparable incomes filling together. The rationale for this deduction is now stronger than ever, as the number of those families has continued to grow. We are especially concerned about the burdensome effect of eliminating this deduction on married couples with moderate to low earnings, typically those who are just starting their work careers.

The conversion of the child care credit to a deduction would likewise result in a greater tax burden on many low and middle-income two-earner families, as well as low income single parents. These are the families that are in greatest need of relief; yet the change would grant a deduction worth $1,680 to a family with an income of $50,000, but only give a deduction worth $720 to a family with half that income. We strongly urge this Committee to keep the child care credit in place.

We also oppose the elimination of the charitable contribution deduction for non-itemizers; we see no reason, either of equity or simplicity, why itemizers should be allowed to deduct their charitable contributions, but non-itemizers should be denied the same privilege.

Likewise, we urge you to retain two mechanisms in current law designed to encourage the participation of American citizens in the political process — the credit for political contributions and the Presidential campaign checkoff. The proposed elimination of the Presidential campaign checkoff is particularly objectionable, since this provision does not entail any tax expenditure. The President's objective seems to be to undermine the system of public financing for presidential elections, which he has always opposed. We believe that public financing of presidential elections has proved to be one of the most successful of the "Watergate reforms." The UAW therefore urges Congress not to tamper with this provision.

The UAW is also opposed to the President's proposal to impose a "floor" on the deductibility of certain legitimate employee business expenses, including union dues. This unfair proposal would wind up denying most workers the right to deduct their small amounts of legitimate business related expenses, while still permitting upper income earners to deduct unlimited amounts of business expenses above the "floor".

Corporate Tax Provisions

The UAW is pleased that the President has apparently recognized that corporations must carry a greater share of the tax burden. Largely as a result of the Administration's 1981 tax legislation, between 1981 and 1983, 128 major corporations paid no corporate income tax or else received rebates from the federal government in at least one of the three years. Seventeen corporations paid no corporate income tax or received a rebate from the federal government in all three years, including such profitable enterprises as General Electric, Boeing, General Dynamics, Lockheed, Grumman, Dow Chemical, Tenneco, and others. The public outcry about this state of affairs is totally justified; the proposal by the Administration to reverse some of the outrageous actions taken in 1981 with respect to the corporate tax base is welcome.

Still, the initiatives in this area do not go far enough. The changes call for corporations to provide 21.7 percent of the total income tax receipts of the federal government in 1990. Without tax reform, that share would be 17.6 percent. However, the share was 23.2 percent in 1979, so that even after reform, corporations would not be footing the same percentage of the tax bill as they were just before President Reagan came to office. Furthermore, the President's proposals with respect to the taxation of corporations reflect substantial "backsliding" from those initially advocated by the Treasury Department: while the latter would have raised an additional $44.7 billion from corporations in 1990, the President's proposals would raise an additional $25.2 billion from corporations, or only 56 percent as much.

Perhaps the biggest disappointment in the President's program is the treatment of capital gains. Not only has the President discarded a sound proposal in the Treasury Department's plan, which would have raised $2 billion from corporations in 1990. On the individual side, he is effectively proposing to widen the loophole that the wealthy are currently enjoying, by reducing the top rate on capital gains from 20 percent to 17.5 percent. We strongly urge this Committee to take steps to eliminate the unfair distinction between taxation of earned versus unearned income by closing the capital gains loophole.

We are disappointed in the provisions in the President's plan relating to depreciation schedules, which substantially cut back on the reforms that were originally suggested by the Treasury Department. The rationale for changing to ACRS in 1981 was that the cost recovery system then in existence resulted in the overtaxation and discouragement of capital investment, thus contributing to the slowdown in productivity. While ACRS, in combination with the investment tax credit and other measures, removed a large number of corporations from the tax rolls, the much awaited investment superboom and jump in productivity did not materialize. Instead, as shown in a recent study by Citizens for Tax Justice, companies that took advantage of the changes made by the 1981 tax legislation to lower their taxes wound up reducing their investment more than the average. Ironically, the highest taxed companies actually increased their investment. Furthermore, official Bureau of Labor Statistics figures show that in both the business and manufacturing sectors, the average rate of productivity growth during the current recovery has lagged substantially behind the average for previous postwar recoveries.

This evidence reinforces our long-held belief that investment growth follows from economic growth and a healthy level of demand for industries products. Tax gimmicks do nothing but waste taxpayers' dollars, starve needed government programs, distort investment patterns and fill corporate coffers and stockholders' pockets. We therefore urge this Committee to make more extensive reforms in the current cost recovery system (ACRS) than advocated by the President.

In spite of the much avowed goal of making the tax code more "neutral" in its treatment of different industries, the subsidies to the energy industry have been left all but intact by the President's proposals. While the Treasury Department's original proposals would have raised almost $6.5 billion in 1990 by closing the special loopholes in this area, the President's proposals would raise less than $1 billion in 1990 from this undertaxed industry. The oil and gas industry has been enjoying massive subsidies from American taxpayers for far too long. We urge the Committee to put an end to that situation.

The UAW supports the President's proposal to repeal the investment tax credit. We believe investment incentives should only be available on a case by case, targeted basis, where it can be shown that this will encourage reinvestment and industrial rebuilding rather than plant closing and plant relocation; prevent industrial and community disruption; create jobs in high unemployment areas; or fulfill a national need as defined by Congress. The investment tax credit, which is bestowed on corporations without any quid pro quos, simply involves giving away taxpayers' dollars in the pursuit of investment spending which more often than not would have been forthcoming anyway.

We apply the same analysis to incentives for research and development. The R&D tax credit is not an effective or efficient means of stimulating needed research and development expenditures by the private sector. As with the credit for capital investments, companies are able to reap the benefits of the research and development tax credit for expenditures that would have been incurred anyways in the normal course of business. We believe that a better approach would be for the federal government to target assistance to specific firms, projects and universities through a program of grants. Assistance could thus be directed where it is truly needed in order to develop new technologies to make the U.S. more competitive and productive. We oppose the extension of the R&D credit for three more years, as proposed by the President. However, if this credit is retained, at a minimum it should be structured to provide some assurance that it will lead to job-creating investments in the United States, rather than being diverted into overseas production and profit.

The UAW is also opposed to allowing corporations to deduct any portion of the amounts they pay out in dividends. And while we welcome the repeal of the exclusion for dividend income, we note that, on balance, these two provisions concerning dividends result in a loss to the Treasury — and an ultimate gain to stockholders — of $7.3 billion in 1990.

In the area of international tax issues, the President's plan stops far short of what is needed to stop the subsidization of American jobs going overseas. In particular, we have criticized the present practice of allowing multinational companies to take a dollar-for-dollar credit against their U.S. taxes for any taxes paid to foreign countries. This is a loophole which encourages U.S. corporations to produce abroad. The President's proposals to impose a per-country limitation on the amount of the foreign tax credit are a step in the right direction, but this Committee should go further and simply allow corporations to take a deduction for their foreign taxes, just like state taxes and other costs of doing business.

The UAW also urges this Committee to reconsider the provisions of the original Treasury Department plan which would have clamped down on tax abuses by limited partnerships. And we believe that the President's proposal relating to a minimum tax on corporations should be expanded, so as to insure that all corporations pay their fair share of taxes.

Conclusion

In conclusion, the UAW appreciates the opportunity to present its views concerning President Reagan's comprehensive proposals for tax reform. While some of his proposals would be reforms in the true sense, others represent a gross misapplication of that term to cover a thinly-veiled pursuit of inappropriate social and economic policy goals having nothing to do with tax reform. The President's proposal simply represents the starting point on the quest for true tax reform. Congress will have to examine the proposals in detail, with an eye towards making those changes which will contribute to the goals of fairness, simplicity and economic growth. We hope this Committee will consider the various recommendations set forth in our testimony for improving the President's plan. We look forward to working with the Members of this Committee as it proceeds with the task of drafting tax reform legislation. Thank you.

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STATEMENT BY RICHARD W. CORDTZ, INTERNATIONAL SECRETARY-TREASURER, SERVICE EMPLOYEES INTERNATIONAL UNION, AFL-CIO, WASHINGTON, DC

Mr. CORDTZ. Thank you, Mr. Chairman.

I am pleased to have with me our chief economist, Peggy Connerton; and Jerry Pellist, our legislative director.

I am Richard Cordtz, the international secretary treasurer of the Service Employees International Union, and president of Local 79 which represents nearly 18,000 building service and health care workers in the Detroit area. On behalf of our international president, John J. Sweeney, and the 850,000 members of the SEIU, I want to thank you, Mr. Chairman, and the members of the Senate Finance Committee for inviting us today to share our views on tax reform.

I would like to emphasize that SEIU has long been an advocate of Federal tax reform. Over the past decade the Federal tax system has become increasingly unfair. Because so much income is sheltered in one way or another, we have much higher tax rates than necessary on what is left, primarily wages. We are pleased that the President and many Members of Congress from both parties now recognize that our loophole-ridden tax system has become grossly unfair and requires a major overhaul.

SEIU strongly supports increases in the personal exemption, the zero bracket amount, and the earned-income tax credit. Together, such proposals will remove the burden of Federal income tax from working Americans below the poverty line and make the tax system fairer for millions of moderate and low income Americans.

At the same time, a number of proposals in the President's tax plan undermine the ultimate prospects for a fair tax reform. In particular, SEIU strongly opposes the taxation of health care benefits as unfair, unfair to American workers who have always paid full taxes on their wages.

Health care is not a rich man's benefit. The President's plan will require 90 percent of American workers to pay new income taxes on about 19 percent of their health benefits. Nearly 80 percent of these workers covered by the health insurance plan earn less than $25,000. The long struggles our low-income members have engaged in at the bargaining table to win health insurance and coverage would be severely eroded if such a tax was imposed. Our locals, which cover mostly low-wage service workers, do not have Cadillac benefit plans and have been aggresive about instituting health cost containment measures.

The President's new plan goes a giant step furter in shifting tax burdens onto the backs of low- and middle-income working people.

Let me emphasize that we strongly reject any plan to tax health benefits. As a union which represents many low-wage working men and women, any tax increases affecting our members causes us great concern. Increases in Federal taxes at this time are especially unfair, since low-income working people have already been forced to grapple with cutbacks in public services over the last 4 years, during which Federal tax reduction efforts have channeled billions of dollars to the very wealthy in our society and to the corporate sector.

We believe that taxation of health benefits would act as a general disincentive to the provisions of health insurance in the future, and as a result would severely impair the ability of working people and their families to achieve and maintain access to quality health care.

Still other proposals in the President's plan undermine the cause of genuine tax reform. For instance, repealing the deductibility of State and local taxes imposes a double tax and unfairly penalizes workers in high-tax States. At a time when State and local governments are struggling to simply maintain public services in the face of cutbacks in Federal aid, eliminating deductibility would increase the pressures for lowering State and local taxes. The added burdens imposed on States confronting high levels of unemployment and slow economic growth would further exacerbate their economic and fiscal hardships. In our view, this proposal is a thinly disguised attempt to impose the Reagan federalism, increasing the responsibilities of the State and local sector while decreasing the financial capabilities of those jurisdictions, an approach rejected by Congress in the past.

Moreover, this proposal is hardly tax reform; it is better characterized as further steps toward dismantling the network of vital social programs that has taken decades to construct. It is simply a threat to the fiscal and economic stability of the State and local governments.

SEIU has also strongly opposed the taxation of unemployment insurance and workmens compensation. Why compound misery of joblessness and disability by further taxing these meager benefits?

The President's proposal also falls short of the major overhaul needed to end the unfair corporate loopholes now given to oil, gas, stock, and real estate speculators and banks.

The CHAIRMAN. I will have to ask you to conclude, also, Mr. Cordtz.

Mr. CORDTZ. Yes.

Mr. Chairman, again I want to thank you and the other members of your Finance Committee. There are several things here we would like to refer to—dropping the provision to tax employer-paid health insurance, and workers compensation and unemployment insurance. We feel that a tax plan that would be fair to everybody in this country would be if every corporation paid the kind of taxes that General Motors does.

You have heard from the other speakers, and we thank you very much for giving us this opportunity to testify.

The CHAIRMAN. Do you mean to say what is good for General Motors is good for the country?

Mr. CORDTZ. No, my name isn't Charlie Wilson. [Laughter.]

The CHAIRMAN. Mr. Carlough.

[Mr. Cordtz's written testimony follows:]

SERVICE EMPLOYEES
INTERNATIONAL UNION, AFL-CIO, CLC
1313 L STREET N.W. • WASHINGTON, D.C. 20005 • (202) 898-3200

JOHN J. SWEENEY
INTERNATIONAL PRESIDENT

RICHARD W. CORDTZ
INTERNATIONAL SECRETARY-TREASURER

TESTIMONY OF THE

SERVICE EMPLOYEES INTERNATIONAL UNION, AFL-CIO, CLC

BEFORE

THE HONORABLE BOB PACKWOOD
CHAIR

FINANCE COMMITTEE
U.S. SENATE

President's Reagan's Proposals for Comprehensive Tax Reform

July 24, 1985

SUBMITTED BY:

Richard W. Cordtz
International Secretary-Treasurer
Service Employees International Union, AFL-CIO, CLC

Statement of Richard W. Cordtz
International Secretary Treasurer
Service Employees International Union, AFL-CIO, CLC

I am Richard Cordtz, International Secretary Treasurer of the Service Employees International Union, and President of SEIU Local 79 which represents nearly 18,000 building service and health care workers in the Detroit area.

On behalf of our International President John J. Sweeney and the 850,000 members of SEIU, I want to thank Senator Packwood, Chair of the Senate Finance Committee, for inviting us today to share our views on the "simple tax" proposals.

At the outset, let me emphasize that SEIU has long been an advocate of comprehensive federal tax reform. Over the past decade, the federal tax system has been archaic and increasingly unfair. Because so much income is sheltered in one way or another, we have much higher tax rates than necessary on what's left -- primarily wages. People who make money by working for a living are paying higher and higher taxes, while people who make money because they have money are paying less and less. Many of our largest corporations -- General Electric, W.R. Grace, General Dynamics, Dow Chemicals, -- also pay little or nothing on billions in profits.

The 1981 Reagan tax cuts accelerated this tax shift. Taking into account inflation and higher social security taxes, low and moderate income workers faced tax hikes, while people making more than $200,000 saw real tax cuts averaging $60,000 or 15 percent in the first three years. Unfair tax policies that shift ever larger tax burdens onto wage-earners are a threat to the income of workers and their families, destroy jobs and economic growth by channeling resources into wasteful and inefficient tax shelters instead of productive investment, and undermine public support for government and the services it provides. Moreover, the loopholes and special tax breaks are causing serious harm to our economy. And, even with those high statutory rates, the current tax system creates severe shortfalls in revenues needed to fund public services.

The right way to simplify taxes and to lower the massive deficits we now face is to close the loopholes that allow so many well-off individuals and companies to avoid paying their fair share in taxes. And by closing those loopholes, we can stop rewarding counterproductive economic behavior. There is no justification for tax loopholes that encourage American firms to relocate plants and jobs overseas, that favor short-term over long-term investments, that make paper manipulation of the tax system more profitable than real economic activity, and that undermine both tax equity and economic growth.

We are pleased that the President and many members of Congress from both parties now recognize that our loophole-ridden tax system has become grossly unfair and requires a major overhaul.

President Reagan's recently announced reform proposal contains many laudible features, but falls disappointingly short of the comprehensive reform America's taxpayers demand.

SEIU strongly supports increases in the personal exemption, the zero bracket amount, and the earned income tax credit. Together, such proposals will remove the burden of federal income taxes from working Americans below the poverty line and make the tax system fairer for millions of moderate and low income Americans.

At the same time, a number of proposals in the President's plan undermine the ultimate prospects for fair tax reform. In particular, SEIU strongly opposes the taxation of health care benefits. This proposal is unfair to America's workers who have always paid full taxes on their wages.

The Administration's position in the debate over fringe benefit tax policy does not square with the facts. In reality, the President's new health tax -- on the first $10 per month of individuals' health premiums and the first $25 for families -- is inequitable and will contribute to runaway deficits in the future. And frankly, it's also poor health policy.

Health care is not a rich man's benefit. The President's plan will require 90% of American workers to pay new income taxes on about 19% of their health benefits. Nearly 80% of these workers covered by health insurance plans earn less than $25,000.

Our union represents thousands of low-wage workers in service industries. The long struggles our low-income members have engaged in at the bargaining table to win health insurance coverage would be severely eroded if such a tax was imposed.

The Administration paints this plan as "less onerous" than the earlier Treasury Proposal. In that plan, workers paid taxes on all employer paid family health premiums above a "cap" of $175 per month and above $70 per month for individual premiums. It's true that the President's new plan raises only about half the $34 billion in total revenue projected over 5 years under the Treasury I plan. However, despite the reduced price tag of the Administration's new approach, it suffers from all the defects of the original plan. The "new floor" is no better than the "old cap". To the contrary, it is a totally regressive tax shift which hits hardest on low and middle income working people.

On balance, this new proposal is worse for SEIU low income members than even the original Treasury proposal. For example, the $175 a month family "cap" would not have touched most of SEIU Local 32B-32J's 65,000 members in

New York, because plan costs averaged only $130 - $140 per month. Similarly, the 8,500 workers in our Chicago Local 25's health and welfare fund would also have been under the $175 "cap". But they will pay now. Now, our members covered by these plans will pay taxes on an additional $120 to $300 a year. The members of both locals are mostly low-wage service workers, who do not have "cadillac" benefit plans, and yet who have been aggressive about instituting health cost containment measures. It will equally affect our Texas nursing home workers who recently fought for health coverage in their first union contract. In short, the President's new plan goes a giant step further in shifting tax burdens onto the backs of low and middle income working people.

Let me emphasize that we strongly oppose any plan to tax health benefits. Even under Treasury I, about half of all SEIU members would be hurt, mostly because they live in high cost regions. For example, the state of California pays $211 per family for health benefits. California Blue Cross premiums average about $250 monthly for family coverage.

The importance of these fluctuations in medical costs by region is underscored by looking at the range of premiums paid for the same benefits in different geographic areas. Contribution rates for family coverage in SEIU's national Health and Welfare Fund range between $117 - $201 monthly. The high cost areas include California, Illinois, Michigan, New York, Ohio and Pennsylvania. The low cost areas are mainly in the South.

There are plenty of other reasons to oppose Reagan's health tax. Taxing employer-provided health insurance would jeopardize our national policy of encouraging essential health care. Neutrality is a general principle of tax reform. But even tax purists accept the tax code as a way to promote desirable social objectives.

On principle, proposals to tax employer-paid health insurance are much more disturbing to us than even a general tax increase. We believe that these tax-based increases in workers' health costs will lead to cutbacks in health benefits. Preventive care, diagnostic services, prescription drugs and eye and dental care are likely targets for the knife. Our low income members would find it difficult to pay the extra money required to maintain these benefits. With the reductions in health services and the rising cost of health care we have already experienced, the ability of low-income people to have equal access to mainstream health services would be severely impaired.

We also believe that taxation of health benefits would act as a general disincentive to the provision of health insurance in the future and, as a result, would severely impair the ability of working people and their families to achieve and maintain access to quality health care.

At a time when the health coverage of Americans is being reduced for the first time in twenty years, the Administration's proposal would create a major new barrier to the goal of expanded coverage. Once in place, such an impediment would likely grow in future years, exacerbating the problem of a dual class health system. Do we really want to return to a 19th century health policy as we approach the 21st century?

Nor will the President's plan control medical costs. Declining quality of care, especially preventive health care, could raise future deficits by leading to more hospitalization and by forcing more people onto the Medicaid rolls. According to the Senate Finance Committee, the federal government would have to spend about $100 billion more to provide the same services that the private sector now provides with about $30 billion a year in tax subsidies.

The only possible rationale for the new healthcare tax is to raise revenues. Yet, the low-income working people who will bear the brunt of this new tax have already been forced to grapple with cutbacks in public services over the last four years, during which federal tax reduction efforts have channelled billions of dollars to the very wealthiest individuals and corporations in our society.

Still other proposals in the President's plan undermine the cause of genuine tax reform. For instance, repealing the deductibility of state and local taxes imposes a double tax and unfairly penalizes workers in high tax states. At a time when state and local governments are struggling to simply maintain public services in the face of cutbacks in federal aid, eliminating deductibility would increase the pressures for lowering state and local taxes. The added burdens imposed on states confronting high levels of unemployment and slow economic growth will further exacerbate their economic and fiscal hardships.

In our view, this proposal is a "thinly-disguised" attempt to impose the "Reagan federalism" -- increasing the responsibilities of the state and local sector, while decreasing the financial capabilities of those jurisdictions -- an approach rejected by Congress in the past. Moreover, this proposal is hardly "tax reform". It is better characterized as a further step toward dismantling the network of vital social programs that it has taken us decades to construct. It is simply a threat to the fiscal and economic stability of state and local governments.

We also believe that there is a strong fairness case for allowing deductions of state and local taxes. After all, charitable deductions would be allowed under the President's plan on the theory that the benefits of giving money to charity can't be spent or saved by the taxpayer and that the dollars go to support activities that serve the public welfare. The same theory applies to state and local taxpayers with the additional caveat that unlike charities where giving is voluntary, individuals must pay state and local tax bills. On these grounds, we strongly encourage the Committee to reject this proposal to eliminate deductions for state and local taxes.

SEIU also strongly opposes the taxation of unemployment insurance and workers' compensation. Under current law, unemployment benefits, which average only $119 per week nationwide, are already subject to taxation if income exceeds $12,000 for singles and $18,000 for married taxpayers. Workers' compensation benefits are woefully inadequate to meet the day-to-day needs of disabled workers and their families. Why compound the misery of joblessness and disability by further taxing these meager benefits?

The President's proposals also fall way short of the major overhaul needed to end the unfair preferential treatment given oil and gas, stock and real estate speculators and banks. Also, the capital gains loophole is expanded and the new "Capital Cost Recovery System" for asset depreciation will eventually be more costly than the current accelerated depreciation scheme.

The end-result is that over the long term, when temporary gimmicks in the plan have run their course, the Reagan program will achieve only a token 9% hike in corporate taxes. This is woefully inadequate as a matter of fairness. It is also a long-term revenue drain. With corporate taxes accounting for only one-sixth of all income taxes under current law, it will not pay for a 7% cut in individual taxes. Even with highly optimistic assumptions about steady economic growth, the Reagan arithmetic on taxes is imbalanced -- with $13 billion in new red ink projected over the next 5 years.

Finally, wealthy taxpayers will once again get the largest percentage tax cuts. The Center on Budget and Policy Priorities notes in a recent study that the average taxpayer over $200,000 will receive a tax cut of $9,250. By contrast, persons with incomes below $30,000 a year would receive average gains of less than $150 a year. As a percent of income, this average tax cut is also highest for the very wealthy. And most unsettling, this tax reduction windfall for the very wealthy is even greater -- by $2,400 --than under the original Treasury proposal. Frankly, these Americans already got more than their fair share of tax cuts in 1981 and do not need or deserve further cuts at the expense of other taxpayers.

SEIU believes that genuine tax reform could go much further in reversing the tax shift that has taken place over the past decade. This tax shift has slashed taxes on the very wealthy by more than one-third and decimated the corporate income tax, while taxes on working Americans have gone up. Moreover, more must be done to restore the federal government's revenue-raising capability in order to control soaring deficits.

Specifically, we urge Congress to adopt the following changes to the President's proposal to achieve these important goals:

(1) Drop provisions taxing employer paid health insurance, workers' compensation and unemployment insurance;

(2) Drop the provision denying deductions of state and local taxes;

(3) Adopt a depreciation system based on the real economic lives of plant and equipment as in the original Treasury plan, and close other special interest loopholes; and

(4) Adopt maximum tax rates for wealthy individuals and corporations of 40%.

These major changes would provide greater tax cuts for low and moderate income Americans beyond those proposed by the President. In addition, instead of adding to the deficit as the President's plan proposes, this approach would raise sufficient money to close the federal deficit gap.

To give you an idea of the possible revenue gains, a single change that ties tax depreciation schedules to the economic life of business assets would add $174 billion more in federal revenues over 5 years compared to the Reagan plan. Also, we believe that you can raise significant money by combining some downward adjustments in individual tax brackets and rates to give greater tax relief to middle income families with a higher top personal tax rate of 40%, perhaps for personal income above $100,000. Such a plan could generate perhaps another $50 billion in new revenues over 5 years. There would be no need to tax employer - provided health insurance and unemployment and workers' compensation benefits. We would also keep state and local tax deductions. At the same time, middle-income taxpayers could enjoy a larger tax cut than under the Reagan plan.

We urge the Congress, starting with this Committee, to embrace genuine reforms that redress the inequities of our current system, put the tax shelter industry out of business and restore the corporate tax to a fair share of federal revenues. A fair tax system, based on the ability-to-pay principle, is essential to assure economic justice for working people, to build a strong, growing economy, and to provide adequate funding for essential public services.

Such a truly comprehensive reform would promote fairness, restore taxpayer confidence, and encourage economic growth by forcing wealthy individuals and companies to stop looking for tax shelters and go back to making money the old-fashioned way - by earning it.

STATEMENT BY EDWARD J. CARLOUGH, GENERAL PRESIDENT, SHEET METAL WORKERS INTERNATIONAL ASSOCIATION, WASHINGTON, DC

Mr. CARLOUGH. Mr. Chairman, I appreciate the opportunity to come before you this morning on behalf fo the 152,000 members and families of the Sheet Metal Workers International Association. I have prepared testimony which I have submitted to the committee, but in listening to the colloquoy that occurred this morning between yourself and President Kirkland, and then after listening to some of the thoughtful questions raised by Senator Mitchell and Senator Bentsen, I believe it would be prudent of me to use the few minutes that I have here this morning to address one issue that I raised in the testimony, and it is a question of taxing of employee benefits.

I believe, Mr. Chairman, you used the word "intransigent" in your discussions with Lane in describing the position of the President at one point on that question. Well, it is a free country, and if the President of the United States can be intransigent on this issue, so can the more humble, less exalted office of the president of the Sheet Metal Workers International Association.

We feel that whether the approach is through a floor, such as is now incorporated in Treasury 2, or through a ceiling, which was the proposal in Treasury 1, that both proposals are just totally unfair. If you have the approach that you have now, you are kicking the building service people, you are kicking the Amalgamated Clothing & Textile Workers. By the way, there aren't any Cadillac plans in health care. There are a lot of Ford plans, but we are all paying Cadillac prices, you know, to the insurance companies. We don't want to kick those people. We don't want to be kicked ourselves; and we don't have a Cadillac plan, either.

Senator, we just finished negotiations—Richard Grandmaison—in the State of Maine. It was successfully concluded—not too much money, because there isn't too much money for union construction workers up in Maine this year. It appears that about 32 percent of the rather modest increase that we obtained at the bargaining table is going to go, in Local 545's health and welfare fund, merely to maintain existing benefits. We don't have any control over that sort of situation.

I saw Senator Bentsen here earlier. In Houston, TX, we just finished negotiations; 32 cents out of some 52 cents had to go merely to maintain local health and welfare benefits.

We can't control costs right now, in the structure in this country, and if you want to control medical costs, there is a lot of pending legislation, a lot of pending bills that have been introduced in the U.S. Senate and in the House of Representatives that would meet this need.

Again, on cost control and the frustration of trying to deal with it as a union representative, in March of this year we established a program to fill in all Medicare gaps for our membership, a very comprehensive program. Our railroad members cannot participate in this program, because they are not covered under our national pension plan; they are covered under a railroad program. An insurance company has offered the same coverage that our union provides to our railroad members at $68 a month. We are providing this coverage, available to our 14,000 retireees, at $13 a month. partly subsidized through our national pension fund, but partly because, since it is a national program and we can talk directly to doctors and the vendors and the providers of services, we have enough clout in order to control costs. But that is a unique situation. In the rest of the movement we don't have that kind of clout in terms of controlling medical costs.

And the future? I have watched the President and the administration and the Congress wrestling, and still wrestling, the whole question of budget deficits. We still haven't come to grips with that problem. Someday even this President is going to understand that additional sources of revenue are going to be necessary to put the fiscal house of this country in order.

If we start with a "modest" tax on health care, the faucet drips a little bit. You will keep coming back to this faucet in the Congress and in the administration to take care of future budget deficits. It won't stop with $10 a month or $25 a month. It will start there, but it won't end there. I know this. I understand this. And because I do, I must be intransigent on behalf of my membership on the whole question of taxation of health benefits.

And on a related matter, I want to congratulate the chairman for the fantastic job that you have performed on the whole question of prepaid legal. We are in your debt. We have an outstanding prepaid legal program ourselves. We are not in Oregon yet, Senator. We are in New York. We are not in Maine yet; we are in Texas. And I am going to leave with the committee the results of what we have been able to accomplished in the last 2 years, working together with our contractors on the whole question of prepaid legal. It is very comprehensive. It is a Cadillac program, but we are paying Ford prices for it. And we are in your debt, Mr. Chairman. Keep up that good fight on prepaid legal. My members now aren't even afraid of lawyers anymore. [Laughter.]

I still am. I get the bills every month. But we appreciate the wonderful job you have done on that. Thank you very much.

[Mr. Carlough's written testimony follows:]

STATEMENT OF EDWARD J. CARLOUGH

General President
Sheet Metal Workers International Association
before the
Committee on Finance
July 24, 1985

I appreciate this opportunity to testify before the Committee on the impact of the President's far-reaching and ambitious attempt to simplify and reform our tax laws on behalf of the members of the Sheet Metal Workers International Association.

Mr. Chairman, our members welcome the current efforts by the President and the Congress to simplify and reform what admittedly has become an extraordinarily complex system for taxing the citizens of this country. The average middle income taxpayer in a two earner family making $20-$35,000 a year not only has difficulty preparing the form 1040 or 1040A without professional assistance, but once it is prepared, the taxpayer often is dissatisfied with the results. The tax laws are riddled with special tax breaks that enable those wealthy enough to afford tax advice to pay less taxes than the middle income worker. The aggressive marketing of such diverse tax shelters as oyster beds, windmills, and jojoba beans only contributes to the perception of the middle and lower income taxpayer that our tax laws are patently unfair. The dangerous consequence of these evils is, of course, the rush to join the underground economy, destroying our traditional system of voluntary compliance with our tax laws.

Thus, efforts to eliminate this unfairness and the complexity it feeds on are to be applauded, for without them we risk the entire system. The President, moreover, seeks to accomplish this simplification while at the same time significantly reducing tax rates for all taxpayers. But, Mr. Chairman, in his efforts to both reduce tax rates and broaden the income tax base to structure a fairer, simpler system, the President will produce a system for taxing our citizens that has some of the same dramatically inconsistent and inequitable results as are contained in the present system.

First, Mr. Chairman, I think the Committee should carefully examine who is getting most of the benefit of the rate reductions. It is certainly appropriate that those of our citizens living below the poverty level should not have to pay tax. The 35.5% average tax reduction which the President anticipates that those earning less than $10,000 would receive under his proposal certainly contributes to eliminating what has been an embarrassing inequity in our tax system.

At the other end of the spectrum are the extremely wealthy. The President anticipates that his proposal will enable them to enjoy an average reduction in taxes of 10.7%. While less than the average benefit extended to the lowest income earners, it exceeds that afforded to the middle-under current law. This inequity is compounded by our regressive system for assessing Social Security taxes. In fact, our workers are facing payroll tax increases right through the end of this century. The combined effect under the President's plan is to place an increasingly disproportionate burden on that segment of our population that is the hardest working and greatest provider of Federal tax revenues.

While this is disturbing in itself, Mr. Chairman, consider the consequences for middle-income taxpayers when some of the President's other base-broadening changes are made. The elimination of the State and local tax deduction, and the two-earner deduction, the imposition of a floor for employee business expenses and other miscellaneous deductions, the limitation on consumer interest deductions, and the conversion of the child care credit to a deduction all could adversely affect the middle income taxpayer.

Most significant for our members, however, is the President's proposal to limit the exclusion for employer-provided health insurance. As you know, Mr. Chairman, the President proposes to tax employer contributions to a health plan up to $10 per month ($120 per year) for individual coverage, or $25 per month ($300 per year) for family coverage.

When this is considered in conjunction with the most favored beneficiaries of the rate reductions, it isn't hard to understand why our members are asking -- "How can the President possibly characterize his proposal as fair?"

Even a more neutral analysis of the health benefit floor would inevitably lead to the conclusion that the proposal is seriously and inherently flawed. First, it is clearly regressive since the contributions eligible for inclusion represent a greater proportion of the income of those at the lower end of the income scale. Moreover, the proposal must perplex the "market force" health economists who, together with the President, have always touted the limitation on the amount of tax-free employer-provided health insurance as a revolutionary means to control skyrocketing health care costs. Taxing the first $10 or $25 a month offers precisely the opposite incentive -- encouraging employers to provide more coverage which will be tax-free, to compensate for the taxable portion.

Mr. Chairman, the Sheet Metal Workers International's concern over the President's proposal to tax a portion of the employer's contribution to an employee's health plan is even more fundamental than this. In a world of federal budget deficits which appear difficult to control and eliminate ultimately through spending reductions, we would be derelict in our leadership responsibilities to our members not to recognize the inevitability of a tax increase sometime in the relatively near future. And what would be an easier source of revenue than taxing additional amounts of employee benefits, whether health, life, or pension? Our members remain vehemently opposed to the taxation of employee benefits. Over the years our tax laws have encouraged employers to fill the void left by the government in fulfilling certain basic needs of our working citizens. Employer-provided health insurance, for instance, relieves government of the burden of supporting citizens when catastrophic or serious illness depletes their resources. Our system of encouraging the provision of private health insurance by employers has contributed to the well-being of most of our citizens. Data collected by the Bureau of the Census in 1983 for the Department of Health and Human Resources and the Employee Benefit Research Institute indicate that more than 59% of all civilian workers, and more than 83% of all full-time employees over the age of 25, have health insurance coverage. Moreover, 45.2% of all those with health insurance coverage earned between $10,000 and $25,000 per year in 1983, 17.1% between $25,000 and $50,000, while only 2.8% of all those with health insurance earned over $50,000 in 1983.

These figures vividly demonstrate the widespread acceptance by the private sector of the importance of providing health and similar protections to most workers. It further demonstrates how we as a nation have come to rely on employer-provided benefits to meet recognized needs and social goals. Even the President has implicitly recognized the unique role of our country's employers in this effort by retaining the tax-free status of certain other employee benefits or vehicles to provide them, such as group life, group legal services, educational assistance, voluntary employee beneficiary associations (VEBAs) and cafeteria plans. For that recognition, we are obviously appreciative.

Moreover, the widespread provision of these benefits means that attempts to tax any portion of them will directly affect the middle-income worker -- that taxpayer who not only benefits the least from the President's rate reductions, but who was also overlooked when the tax incentives for narrow groups of taxpayers, which the Treasury Department's November proposal would have repealed, were restored by the President. Perhaps the revenue lost due to deletion of the health floor proposal could be recovered by examining the provision of current law permitting taxpayers to expense intangible drilling costs, the liberalized capital cost recovery rules, the restored capital gains exclusion, the extension of the research and development credit, or even the 33% corporate rate.

Mr. Chairman, I will conclude my statement by urging you and your Committee to consider carefully the testimony you have heard over the past several months. There have been other complaints about the impact of various parts of the President's tax reform proposal on specific transactions, industries, and narrow groups of taxpayers. You may not have heard, however, from the hard-working taxpayers like our members who are bearing most of the burden, but receiving the least of the benefits and who will, in fact, experience hardship under the guise of fairness and simplicity.

I thank the Committee for the opportunity to present the Association's views.

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CABLE DEWBALAW

July 24, 1985

Ms. Betty Scott-Boom
Committee on Finance
U.S. Senate
SD-219
Washington, D.C. 20510

Dear Betty:

Enclosed is the information on prepaid legal services to which Mr. Edward J. Carlough, General President, Sheet Metal Workers International Association, referred in testifying before the Finance Committee today. It is my understanding that the Committee agreed to its insertion in the record of today's hearing.

Thank you in advance for your assistance in ensuring that this material becomes a part of the record of today's hearing.

Sincerely,

Jayne F. Boyle

Enclosure

cc: Larry Cassidy

A FACT SHEET ON THE INTERNATIONAL TRUST FOR LEGAL SERVICES

Background. Since the AFL-CIO first endorsed the concept in 1972, teachers, laborers, teamsters, auto workers, clerks and other unions have set up all kinds of legal service plans. The Sheet Metal Workers International Association, however, is the first to establish a national plan providing extremely comprehensive legal services.

Legal Service Benefits. The plan covers virtually every type of personal legal service the average person needs. There are no co-payments, deductibles or waiting periods. There are no limits on the number of times a member may see an attorney. Plan services include:

TELEPHONE ADVICE OR OFFICE CONSULTATIONS - SEPARATION & DIVORCE
MORTGAGES - REAL ESTATE - BANKRUPTCY - LANDLORD/TENANT - DEEDS
DEBT DEFENSE INCLUDING: REPOSSESSION, GARNISHMENT, FORECLOSURE
ADOPTIONS - WILLS - POWERS OF ATTORNEY - NOTES - NAME CHANGES
MISDEMEANORS - EXPUNGEMENT OF CRIMINAL RECORD - JUVENILE CASES
DEFENSE OF FELONIES OR ANY CIVIL SUIT - CONSUMER MATTERS
REDUCED FEES ON WORKERS' COMPENSATION, PROBATE & PERSONAL INJURY

Tax Return Preparation. The plan also covers the preparation, by H & R Block, of the members' individual or joint state and federal tax return.

How Services Are Provided. The International Trust for Legal Services conducted lengthy interviews with several firms before selecting Hyatt Legal Services, a nationwide law firm, to be the exclusive provider of services.

Hyatt Legal Services was founded six years ago. Today, it is the largest general practice law firm in the country, with 175 offices in 21 states. Hyatt Legal Services specializes in representing individuals, not corporations or businesses.

Where possible, services will be provided using a "legal HMO" approach:

- In communities with Hyatt Legal Services offices, members will use any Hyatt attorney in any Hyatt office.

- In communities where Hyatt does not yet have offices, members will be served either:

  a) by one or more carefully selected Participating Law Firms supervised by Hyatt Legal Services; or

b) by attorneys selected by the members themselves; members will be reimbursed for legal fees according to a schedule established by the International Trust.

The number of members in each local will determine whether a Participating Law Firm will be designated. If a member uses either a Hyatt Legal Services office or a Participating Law Firm, the member's case will be covered completely, no matter how time-consuming or complex it may be. The member will never be asked to pay "additional" legal fees.

Hyatt Legal Services is glad to have suggestions for Participating Law Firms from Sheet Metal Locals. However, these firms must meet Hyatt Legal Services' standards and be willing to abide by Hyatt's prepaid rules and procedures.

How To Use The Plan. The eligibility standards are very similar to health and welfare eligibility requirements, requiring 400 hours worked in a four-month period. Each month, the International Trust provides Hyatt Legal Services with a list of eligible members. To use the plan, members call Hyatt Legal Services toll-free to check their eligibility. In this way, the member's problem remains confidential.

Hyatt Legal Services then gives the member an Authorization Number over the telephone. By giving the Authorization Number to a Hyatt attorney or a Participating Law Firm, the member is entitled to receive services immediately.

Members who must select their own attorneys are mailed a claim form. They are reimbursed for their attorney's fees, up to prescribed maximum amounts, as soon as they send the claim form and a copy of the lawyer's bill to Hyatt Legal Services.

Funding. Participation in the International Trust for Legal Services and Prescription Drugs requires a direct 15¢ contribution from the employer to the Trust. Employers can use the same transmittal form presently used for pension plan contributions.

Sources of the funding include:

a) Future collective bargaining agreements;

b) Scheduled increases resulting from prior collective bargaining negotiations; and

c) Monies in a health and welfare fund.

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HYATT
LEGAL SERVICES

SHEET METAL WORKERS INTERNATIONAL TRUST
TABLE I - PARTICIPATING SHEET METAL WORKERS LOCALS
September 1, 1982 through December 31, 1984

Services Began	Service Area	Local Union	Average Eligibles Since Start
09/82	*CT-Fairfield County	39	191
11/82	IL-Decatur Area	133	174
11/82	*SMWIA-INT		85
12/82	LA-Lake Charles	196	60
02/83	HI-Honolulu	293	375
03/83	NY-New York City, Long Island & New Jersey	28	2080
05/83	WI-Janesville	18	15
10/83	OH-Columbus (Specialty)	98	51
11/83	NY-Elmira	112	159
12/83	NY-Syracuse	58	245
12/83	IL-Champaign/Urbana	230	103
01/84	CA-Riverside, San Bernardino	84	175
01/84	IL-Springfield	84	128
03/84	*TX-Houston	54	1241
05/84	MI-Saginaw	408	139
06/84	KS-Topeka	77	69
08/84	WA-Seattle	99	640
08/84	WA-Tacoma	150	174
09/84	MI-Detroit (Specialty)	292	78
12/84	*CA-San Francisco	104	2205
12/84	*CA-Fresno	371	470
12/84	*CA-Stockton	283	267
12/84	*SA-Sacramento	162	263
12/84	WA-Yakima/Tri-Cities	242	78
12/84	TX-El Paso	49	27
Various	Specialty Agreements		50
		TOTAL	9542

* Retirees of these locals are also covered for full plan services. Approximately 1,000 retirees were eligible for services as of December 31, 1984.

TABLE II - SERVICE DELIVERY SUMMARY
As of December 31, 1984

Locals Served by Hyatt Legal Services	Number of HLS Offices		December Eligibles
SMW International	8		81
Local 98 (Columbus)	3		13
Local 54 (Houston area)	8		1416
Local 99 (Seattle area)	5		611
Local 150 (Tacoma)	1		250
Local 104 (San Francisco/Alameda Co.)	12		2000
Local 292 (Detroit)	10		74
		TOTAL	4445

Locals Served By Participating Law Firms	Number of Firms/Offices		December Eligibles
Local 133 (Decatur)	2		266
Local 293 (Honolulu)	2/3		371
Local 28 (NY City-No. N.J.)	14/17		2438
Local 230 (Champaign/Urbana)	3		154
Local 112 (Elmira)	2		198
*Local 58 (Syracuse)	2		304
Local 84 (Springfield, IL)	2		143
Local 509 (Riverside, San Bernardino)	2/3		196
Local 408 (Saginaw/Midland/Bay City)	4		190
Local 77 (Topeka)	1		77
Local 49 (El Paso)	2		27
Local 242 (Yakima/Tri-Cities)	6		78
Local 371 (Fresno)	2		470
*Local 283 (Stockton/Modesto/Tulare)	5		267
Local 162 (Sacramento)	2		263
		TOTAL	5442

Locals Served by Fee Reimbursement		December Eligibles
Local 104 (No. Cal. retireds)		205 (est.)
Local 39 (Fairfield County, CT)		284
Local 196 (Lake Charles)		52
Local 18 (Janesville, WI)		21
Various Specialty Agreements		34
	TOTAL	596
	GRAND TOTAL**	10,483

* Hyatt Legal Services will soon be opening offices in the following cities: Syracuse, NY (June, 1985); Sacramento, CA (October, 1985); and Stockton, CA (October, 1985).

** Approximately 1,000 retirees were also eligible as of December 31, 1984.

SHEET METAL WORKERS INTERNATIONAL TRUST
TABLE III - USAGE REPORT BY LOCAL UNION
September 1, 1982 through December 31, 1984

LOCAL UNION	NO. OF MONTHS IN PLAN	AVERAGE NO. OF ELIGIBLES	NO. OF CASES CLOSED	NO. OF CASES PENDING	TOTAL NO. OF CASES	ANNUALIZED RATE OF PLAN USAGE
39	28	191	95	31	126	28.3
133	26	174	116	32	148	39.3
INT	26	85	27	20	47	25.5
196	25	60	9	15	24	19.2
293	23	375	28	38	66	9.2
28	22	2080	678	299	977	25.6
18	20	15	3	4	7	28.0
98	15	51	15	2	17	26.6
112	14	159	46	44	90	48.5
230	14	103	17	27	44	36.6
58	13	245	46	42	88	33.2
509	12	175	22	36	58	33.1
84	12	128	25	27	52	40.6
54	10	1241	233	240	473	45.7
408	8	139	14	9	23	24.8
77	7	69	1	5	6	14.9
99	5	640	76	80	156	58.5
150	5	174	16	25	41	56.6
292	4	78	0	0	0	0.0
104	1	2205	8	31	39	21.2
371	1	470	2	6	8	20.4
283	1	267	0	6	6	26.9
162	1	263	1	10	11	50.2
242	1	78	0	2	2	30.7
49	4	27	0	0	0	0.0
Specialty Agmts.	Var.	50	5	4	9	N/A
TOTALS			1483	1035	2518	

SHEET METAL WORKERS INTERNATIONAL TRUST
TABLE IV - REPORT ON CLOSED CASES
September 1, 1982 through December 31, 1984

	Number of Cases				
Casetype	Telephone Only	Consulta-tion Only	Full-Fee Matters	Total	Percent
Documents: Deeds Notes, Powers, etc.	10	1	79	90	6.1
Wills	9	1	268	278	18.7
Adoption	2	1	9	12	.8
Premarital Agreement	0	0	3	3	.2
Divorce	20	14	60	94	6.3
Name Change	0	0	8	8	.5
Real Estate	22	18	187	227	15.3
Landlord/Tenant	12	4	14	30	2.0
Debt Collection Defense	11	3	27	41	2.8
Bankruptcy	4	5	4	13	.9
Consumer Matters	46	11	35	92	6.2
Civil Litigation Defense	20	10	26	56	3.8
Expungement	1	1	3	5	.3
Misdemeanor and Traffic Matters	22	18	158	198	13.4
Felony Defense	2	0	19	21	1.4
Contingent Fee Consultations	22	15	0	37	2.5
Miscellaneous Consultations	171	107	0	278	18.7
	374	209	900	1483	99.9

Note: This table categorizes each case on the basis of the most extensive service provided. Many full fee cases, however, will also involve telephone and/or office consultations.

The CHAIRMAN. What are you paying on the prepaid legal?

Mr. CARLOUGH. Fifteen cents an hour. And it not only includes the most comprehensive possible program you could find—we work with Hyatt Legal Services, Joel Hyatt, an outstanding young person—it includes tax preparation, the most comprehensive kind of legal care, and it also includes a full prepaid prescription. You see, quite often when we get in collective bargaining we sometimes have a fight with our older members and our younger members. The older members want to put more money in the pension, the younger members want to put more money in health care, in the envelope. So what we did, we devised a program that would have appeal to all of our members, at whatever age—the prepaid legal, and the prescription program. And they are working wonderfully well.

The CHAIRMAN. You lost me there for a moment when you skipped from prepaid legal to prescriptions.

Mr. CARLOUGH. The whole package is 15 cents an hour, employer contribution.

The CHAIRMAN. Including prescriptions?

Mr. CARLOUGH. To a national trust fund.

The CHAIRMAN. Including law, including prescriptions? I don't know how?

Mr. CARLOUGH. Including full prepaid prescriptions, without any coinsurance or deductions. And, as a matter of fact, if you are on maintenance drugs we send a 6-month supply to the home of the member and his family. And then we send a reminder after 5 months that they need to renew it.

The CHAIRMAN. You know, for the life of me, I have never understood. Mr. Cordtz in his testimony quoted the Finance Committee study that it would cost the Federal Government $100 billion to provide for the level of health insurance that now employers and employees pay for; sometimes employers pay the full amount, sometimes there is a joint payment from the employees. Unions clearly pioneered this, and other nonunion employers have come along with it. It is actually not a Finance Committee study; it is a study of the Joint Committee on Taxation, which probably even gives it a better presumption of validity than had we studied it. But that is what it shows: If the Federal Government were to try to provide the same level of benefits for your members and for the other nonunion employees in this country that they now get through collectives bargaining or if there is not employer-provided plans, it would cost about $100 billion, and we would have to raise the $100 billion somehow—tax you, tax the employers—I don't know where we would get it; we would have to raise $100 billion to pay for it.

We forgo $30 billion because we don't tax health benefits. Of that, about $23 billion is income and about $7 billion is Social Security. And for that, we get, for most of the employees who working in this country, a very adequate health insurance system. If the Federal Government provides it, you are not going to have the option to change from AETNA to Blue Cross to Continental Casualty as they might choose to give you a better deal; you are going to be insured by the U.S. Health Care Corporation, and that's it. And you won't have any options. And it is probably going to be the same program for the sheet metal workers as it is for the food and commercial workers. There probably isn't going to be much difference between risky industries and different industries. There probably isn't going to be much difference between a union that may be composed principally of younger people and older people.

I bargained labor contracts for 5 years. I represented the employers. And I never, never failed to respect the fact that the union business agents understood their unions very well. They had to run for office just like I have to run for office, and if they didn't quite understand what their members wanted, they didn't stay in office very long. And I was amazed by the fact that bargaining in Portland, OR, for health benefits would be different than bargaining in Medford, OR, for health benefits 300 miles away, even with the same union let alone different unions.

If you get a Federal Government plan, it is going to be unresponsive to geographic differences, unresponsive to demographics and unresponsive to anything else.

You heard the exchange between Lane and I this morning. I don't like the taxation; I hope we don't tax them. And if we do, I want the least tax possible. But we get more value for our money out of bargained benefits than probably any other tax subsidy, if that is what you want to call it, any other tax subsidy that this Government gives.

Senator Moynihan.

Senator **Moynihan**. Well, on just that theme, I guess I ought to ask Eddie, "How do you get to be a member of the Sheet Metal Workers?" [Laughter.]

I guess I am a little old and arthritic for that.

Mr. **Carlough**. I have an extra card in my pocket, Senator, if you would care to apply.

Senator **Moynihan**. Listen, you never know. Heights don't bother me one bit, but lawyers terrify me. [Laughter.]

Just to pick up on the very important remarks the chairman made in regards to the problem with this whole exercise. It really began as a very radical assault on a whole set of agreements that had been built into the Tax Code—such as your particular interest that, as long as we protected the rights of employee health benefits, we would not end up with a U.S. Health Corporation; and for example Mr. Connerton there, could shop around to find the best insurance company—the same kind of thing Eddie does with UAW."

But here we are thinking, "Well, all right, how can we do this?" At first we were going to do really radical surgery. I mean, it was going to make a huge change. Well, now we are trying to make it less radical. But I think it is very generous of Eddie Carlough, who is a generous fellow, to say, "OK, we can live with it." Sheet metal workers are highly skilled persons, and nobody builds buildings overseas yet. So they have got their jobs.

But the service employees? They go right down to the bottom. You know, you have got people working not far from minimum wage, right?

Mr. **Cordtz**. That's very correct, Senator.

Senator Moynihan. That's right. And what you can do for them is to get some of these fringe benefits. Well, the fact is, that $100 or $300 for them is a bit of a whack, right?

Mr. Cordtz. Every dollar in income.

Senator Moynihan. Yes. Those are people who know every dollar they have got in the house, everything they have got in the icebox, you know. And so here we are. That is why I am sort of generally puzzled.

And I thank the UAW for coming to the aid of this issue of State and local taxes. Mr. Cordtz, I think, would be the one most affected. If you greatly diminish the financial resources of State and local government, you diminish the kinds of contracts the SEIU can negotiate. Isn't that right?

Mr. Cordtz. That is right.

Senator Moynihan. It is really going to directly affect your low-income State and local workers.

Mr. Cordtz. Our union and millions of other workers in this country are greatly affected. They are just above minimum wage in many instances, and many of them do not have anywhere near the reference of a Cadillac plan; they probably have the lowest——

Senator Moynihan. The Model-A.

Mr. Cordtz. Well, a Model-A in these times would be worth a lot of money.

Senator Moynihan. I guess so. [Laughter.]

Mr. Cordtz. It could be a Model-T plan, I would say, that many of our members that receive those benefits would be covered by.

As I said earlier, when we talk about Cadillac and talk about a description of plans, I think the addressing of the responsibility of the people of this country to the obligation to have a proper tax program is that we see to it that the corporations such as I mentioned, and I used General Motors as an example, tht if we could get all of the corporations in America to be paying that kind of a tax plan, you gentlemen would not have a hard decision to make in your recommendation in your committee.

Senator Moynihan. I think if I may interpret your comments, what you are really saying is that what is good for General Motors is good for General Electric.

Mr. Cordtz. Yes, and General Dynamics, and many others.

Senator Moynihan. We don't necessarily disagree on this committee, sir.

Thank you, Mr. Chairman. Thank you all for good testimony.

The Chairman. Senator Mitchell.

Senator Mitchell. Thank you, Mr. Chairman.

Mr. Carlough, I appreciated your very forthright and unequivocal statement on the question of health care benefits.

I was interested in your comments that in two recent agreements, one in Maine and one elsewhere, in one case 50 percent and in the other over 60 percent of the increases were devoted to merely maintaining the current levels of health benefits.

Mr. Carlough. That is correct.

Senator Mitchell. That is what you said. Of course, that indicates that your members and all persons in a similar situation throughout the country are affected by the continuing dramatic increases in the cost of health care.

Mr. Carlough. Just about.

Senator Mitchell. And that, of course, has gone on for several years, we are trying, in a separate context, to deal with that.

One of the reasons for that, of course, as every study has shown, is that in the last half century we have largely separated the receipt of health care services from the payment for them. And it is human nature, of course, to utilize more frequently those services which we don't perceive ourselves as paying directly, as opposed to when we do have to.

Mr. Carlough. Excuse me, Senator, if I may. We do pay directly. It is taken out of our wages to go with the health and welfare plan. We pay in one way or another.

Senator Mitchell. That is indirect. A person pays a certain amount, he then gets a health care plan. He pays a certain amount whether or not he receives the health care services. And the specific quantity of health care service by an individual is not directly related to the amount that is paid in premium—that is the point—as opposed to two uninsured persons. If you go in and have an operation, you pay $1,000. If Mr. Cordtz doesn't go in and have the operation he doesn't pay anything.

Now, one of the problems under the existing health care system, of course, is that there are no substantial or significant antidiscrimination rules, so that a high-paid employer, a management person, can receive a much more comprehensive plan than someone who you represent, someone at the lower level. And the original Treasury plan, by exempting a certain amount of income and taxing the amount received above that, was obviously intended to deal with that problem. I understand your objection to that, but my queston is: Your own testimony indicates a very real problem in the increase in health care costs, and even assuming that we accept your position and don't impose a tax, you are going to face a problem in the future. If it is 60 percent this year just to maintain the current level of benefits, unless we take some drastic steps in this country it is not going to be very long until it is 100 percent. And so you are in effect getting nothing except maintaining the current level of benefits.

I have two questions. The first is specific, the second is general. The first is, do you favor, whether or not any tax is imposed, the imposition of some antidiscrimination rules in the health benefit area that would prohibit higher paid persons from getting more desirable plans than those lower paid persons?

Second, I would like your comments in a broader sense on what we do about the rising costs of health care in this country? That is not just a tax matter; it is broader than this tax issue.

Mr. Carlough. In answer to the first specific question, I would need to know how we define "discrimination." If we are defining it by dollar amounts, I would need to know the dollar amounts. The $2,100 that you had mentioned earlier here this morning in reference to Treasury One's proposal of the cap approach would have affected approximately 45 percent of our local unions in the United States in the construction industry at the present time. So, I would need to know the definition of "discrimination," and what dollar level it is pegged to.

Senator **Mitchell**. Well, I will make that clearer in writing. My point is that in other benefit areas, such as pensions, a management employee cannot offer a plan in which he receives a much great benefit merely by virtue of his higher income than a person at a lower income level. My question really is, Do you favor extending that concept?

Mr. **Carlough**. Based on that explanation, I would subscribe to the concept.

Senator **Mitchell**. Now, what about the general subject? You spent a lot of time talking about health care, and I understand it it important to you; it is important to everybody.

Mr. **Carlough**. It is frustrating. It truly is. You see, most of our local unions have local union collectively bargained health plans, and the member is really conscious of the health costs, because, unlike industrial bargaining, they will have benefit amounts—so much for surgery, so much for this and that. We don't. We will negotiate 50 cents an hour, and then the insurance company in Maine will tell Dick Grandmaison, "We need about 32 cents of that to maintain your present level of benefits." So the members consciously have to vote, and they feel they are taking that money out of their pockets. That's why I don't think the cap approach is going to work. It won't discourage the insurance companies from raising their rates.

We have found on our SMW Plus Program that we have been able to get a Medicare Program for our retired members, closing and filling in the Medicare gaps. We have been able to get a better handle on it. We have been able to get a better handle on our prepaid prescription, because we insist on generic drugs being prescribed. And if the doctor won't do it, we tell our members, nicely, "Get another doctor." We have to work together to control these kinds of costs.

When we are dealing with a national program such as our national health plan, and we are talking directly with doctors and hospitals, and urging our members to change if they don't follow certain rules and certain forms and certain charge practices, you feel you can get more of a grip on it. But we are the only union in the construction industry that has a national health plan, for example, so what about all of the others? And what about the other of our members and the building service members and the others that are affected by the thing?

I know there are a number of bills pending like Senator Kennedy's—I don't want to single out the Senator; I know there are a number of other cosponsors—on the whole question of containment of medical costs. It is a serious problem. We would be willing to support virtually any one of the range of bills that we have seen that would at least bring the country to grips with the escalating cost of medical care.

Now, the cost is escalating; but I am not so certain, sir, that the quality and the service is escalating at the same rate, and that bothers me as well. That is another subject.

Senator **Mitchell**. Well, in about 25 years we will have the same surplus of doctors as we now do of lawyers, and then maybe you will get the same results in health care that you are now getting in your prepaid legal programs.

The CHAIRMAN. I have no other questions.

Senator Moynihan.

Senator MOYNIHAN. No, but thanks to the panel for first-rate testimony. Wish us luck.

The CHAIRMAN. George, any more?

Senator MITCHELL. No, thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much.

Now let us conclude with a panel of Keith Geiger, Albert Shanker, William Lucy, Harold Schaitberger, and Moe Biller.

Mr. Geiger, go right ahead.

STATEMENT BY KEITH GEIGER, VICE PRESIDENT, NATIONAL EDUCATION ASSOCIATION, WASHINGTON, DC, ACCOMPANIED BY PAT DIX OF THE GOVERNMENT RELATIONS STAFF OF THE NEA

Mr. GEIGER. Thank you, Mr. Chairman.

I am Keith Geiger, vice president of the National Education Association, and with me is Pat Dix from our Government Relations Staff.

We appreciate the opportunity to present our views on the administration's tax reform plan as it affects education and educational personnel.

NEA agrees that tax reform is urgently needed. On balance, NEA believes that the Reagan plan is an improvement over present law in many of the areas. We strongly support increases in the flat rate deduction for individuals and families, personal exemptions, the expanded earned income tax credit, which would help take families in poverty off the tax roles, and the proposal to make permanent the exclusion of employer-paid educational assistance and group legal services and taxable income.

But in other respects, the administration plan falls far short of tax equity and is actually counterproductive for education at a time when excellence in instruction is a top national priority.

One of the principal concerns is the proposal to repeal the deductibility of State and local income, sales, and property taxes. It would be a huge doublecross on the States and localities which bear the costs of education and other vital public services.

At the present time, total spending annually for public elementary and secondary education is $125 billion per year. The direct Federal share is 6.2 percent, the lowest in 20 years. The States provide 49 percent, local governments provide 44.8 percent.

The States have clearly extended themselves to provide quality education, both in terms of per capita expenditures and as a percent of expenditures for all functions. For education funding, the repeal of deductibility has a very direct impact to a voter. The decision to support or reject a millage election or a State sales tax for education is hardly ever based on, "Is this deductible or not?" The voters' decision to support or reject education is based on a perception of State and local tax burden, and the loss of deductibility would dramatically increase the perception of that burden.

There is a strong base for education funding at the State and local level that should not be undermined by this Federal Government, which is the only partner in education which is not now carrying its share of the load. Federal bugets have failed to keep pace with inflation in recent years. Today, more than half a million students have been dropped from eligibility and now are ineligible for Pell grants or for other programs.

Only 45 percent of the 11 million disadvantaged children who need services under chapter 1 receive them. In 1981 it was 55 percent, and I suspect this might go back to some of the comments Senator Moynihan made earlier about raising a large deficit would reduce the social programs; this is one that it has drastically reduced.

While States have done their part, the Federal share of elementary and secondary funding has fallen from 9 percent in 1980 to the present 6.2 percent.

The administration proposal is a tax increase that it claims would yield an estimated $39 million, which happens to be exactly the amount by which individual income taxes were reduced in the first year of 1981 Economic Recovery Tax Act. According to the Advisory Commission on Intergovernmental Relations, however, the revenue increase would be only $28 billion.

We must oppose the attempt to impose a tax on the first 10 dollars' worth of employer-paid health insurance premiums for individuals, and the first 25 dollars' worth for families. This is one of the most regressive proposals in the whole package. It adds $120 to $300 of nondisposable income for every wage earner to be taxed regardless of income level.

Public education personnel receive low salaries. Their benefits are important to them. Opening the bidding on taxation of benefits would be a further financial pressure against staying in the profession. Pension coverage and health benefits are two of the benefits that to some degree balance the small paycheck. For many teachers and support staff, the taxation of these benefits would be the last straw, forcing them to leave education at a time when serious teacher shortages loom. And as you are all aware, there is a projection for 1 million teachers needed over the next 10 years. I suspect if this passes, you are going to see some of the poorer paid teachers leave now, and you will need more of an increase.

Mr. Chairman, NEA supports tax reform and believes it must promote equity, fairness, and balance. It must assure adequate revenues to finance education and other critical public services. It must be in accord with national priorities, especially the drive for excellence in education, and it must result in a structure that is both workable and acceptable.

For the well-being of public education and the men and women who work in America's schools, we ask that you give particular attention to assuring that the State and local tax deduction continues, that employer-provided benefits remain untaxed, that retirement savings plans continue to offer important benefits to educational employees, and that the two-earner deduction and the child-care credit be retained.

I thank you.

The CHAIRMAN. Thank you.

Mr. Shanker.

[Mr. Geiger's written testimony follows:]

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LEGISLATIVE INFORMATION

STATEMENT OF
THE NATIONAL EDUCATION ASSOCIATION
ON THE ADMINISTRATION'S TAX REFORM PROPOSALS
BEFORE THE
COMMITTEE ON FINANCE
OF THE
SENATE OF THE UNITED STATES
PRESENTED BY
KEITH GEIGER
NEA VICE PRESIDENT
JULY 24, 1985

MARY HATWOOD FUTRELL, President • KEITH GEIGER, Vice President • ROXANNE E. BRADSHAW, Secretary-Treasurer
DON CAMERON, Executive Director
(202) 822-7300

Mr. Chairman and Members of the Committee:

I am Keith Geiger, Vice-President of the National Education Association, representing 1.7 million education personnel in the nation's schools and institutions of higher education. We appreciate the opportunity to present our views on the Administration's tax reform plan as it affects education and education personnel.

NEA agrees that tax reform is urgently needed. In our view, current law is unnecessarily complex and the burden of taxation is not fairly distributed in terms of ability to pay. Our perspectives on this issue reflect a membership that is representative of middle class America. The median age of NEA members is 39. Seventy-two percent are women, and about 73 percent of the total membership is married. Average salaries from school employment range from $17,998 in the Southeast to $23,128 in the West. Total average income, including that of a spouse, is $36,061. Nineteen percent of NEA members live in cities, 30 percent live in suburbs, and 51 percent live in small towns or rural areas.

For tax reform to succeed and be widely acceptable, NEA believes that current proposals to modify the tax code should be measured against the following criteria.

1. Tax reform must promote equity, fairness, and balance.
2. Tax reform must assure adequate revenues to finance education and other critical public services.
3. Tax reform must be in accord with national priorities, especially

the drive for excellence in education.

4. Tax reform must result in a structure that is both workable and acceptable.

The Administration Proposals - An Overview

On balance, NEA believes that the Reagan tax plan is a significant improvement over present law in many areas. We applaud the increase in the flat-rate deduction for individuals and families (zero bracket amount) and personal exemptions, which are long overdue and would be of great benefit to the 65 percent of American taxpayers who do not itemize deductions. The expanded earned-income tax credit would help take families in poverty off the tax rolls. A strengthened minimum tax on the wealthy and on prospering corporations would enhance public confidence in the fairness of the federal income tax system. We strongly support the proposal to make permanent the exclusion of employer-paid educational assistance and group legal services from taxable income.

But in many other respects, the Administration plan falls short of tax equity. It dampens progressivity. Indeed, some of its provisions are more regressive than current law. Since 1981 we have seen a drop in the top marginal rate from 70 to 50 percent, and a further drop to 35 percent is proposed. The top capital gains rate has been reduced from 40 to 20 percent, and a further drop to 17.5 percent is proposed. These lower rates are a boon to millionaires, but not to the average taxpayer. The Administration's own documents show that taxpayers earning more than $200,000 a year would receive a much larger tax reduction in dollar amounts than middle-income taxpayers. And while the Administration makes much of the fact that taxes for lower-income taxpayers would be reduced by as much as 35 percent, this reduction amounts to only $30 for a family of four with an income of $10,000. For the $200,000 income family the tax reduction would be $9,500. These, again, are the Administration's own numbers.

The Administration's proposal would continue indexing income tax brackets, the zero bracket amount, and the personal exemption to reflect annual increases in the Consumer Price Index. Indexing can only compound the difficulties of raising sufficient revenues to pay for government services. This is especially true in light of the estimated $750 billion reduction in taxes enacted in 1981. Retaining indexing at a time when the personal exemption and zero bracket amounts are increased and the marginal rate is reduced to 35 percent will spell trouble for the funding of education and other public services -- including the national defense -- in the future. At a time of ballooning deficits it is apparent that Congress has the obligation to come up with the money for the programs it enacts. The tax reform package cannot be revenue-neutral if indexing continues; tax rates will have to go up to keep the federal deficit from climbing ever higher.

The proposed changes in depreciation rates and the preferential rates on capital gains are touted as economic stimulants. However, we call the Committee's attention to "The Failure of Corporate Tax Incentives," a Citizens for Tax Justice study of the effects of the business investment incentives in the 1981 Economic Recovery Tax Act. The study showed that between 1981 and 1983 the 50 lowest-taxed corporations actually reduced their investment in new plant and equipment. The justifications for tax breaks for business, as consistently proposed by this Administration, are wearing thin. Increasing the purchasing power of individuals is a much more powerful stimulus to the economy, and a truly progressive system does just that.

This testimony will review in more detail the probable effects of this proposal on education and on education personnel.

EFFECT ON EDUCATION

A Critical Concern - The Repeal of Deductibility

One of the principal concerns of the NEA regarding the Administration's proposal is the repeal of the deductibility of state and local income, sales, and property taxes. We believe deductibility goes to the heart of the universally acclaimed effort to achieve educational excellence throughout the nation. Repealing the deduction would destabilize longstanding patterns of intergovernmental funding and raise new and unnecessary obstacles to educational improvement. The *New York Times* aptly terms this proposal a "huge double cross" on the states and localities which bear the costs of education and other vital public services.

Education is a critical element in our country's quest for a knowledgeable citizenry, an expanding economy, and a strong and secure nation. Now is the time we should be seeking new resources to enhance the quality of our schools, not playing with plans that would reduce financial support for public education. The stakes are very clear: education's contribution to our economic vitality, to our place in the international community, to our defense and security, to the lives and opportunities of millions of young men and women. Disinvestment in the education of America's human resources not only jeopardizes our future but threatens the nation's tax base.

The Education Partnership

Since the passage of the Northwest Ordinance in 1785, the federal government has provided crucial leadership and financial support to education as a critical national concern. At the present time total spending annually for public elementary and secondary education is $125 billion per year.

* The direct federal share is 6.2 percent ($8.6 billion).

* The states provide 49 percent ($67.4 billion).

* Local governments provide 44.8 percent ($61.6 billion).

Funding patterns vary according to state laws governing the application of the revenue base to school financing, so these are average figures. The range of direct federal funding for elementary and secondary education in the states is from 3.2 percent to more than 17 percent; the state share, in school aid programs and other forms of support, ranges from eight percent to 91 percent. Reliance on local contributions range from 0.3 percent to 89 percent. A chart showing state-by-state school funding in dollars and percentages from the three levels of government appears as Table I in the appendix.

Over the past 12 years, there have been some interesting trends. The state share of education expenditures has increased from 40 percent to nearly half, while the local share has declined from 52 percent to 44 percent. These changes reflect increasing state commitment to education and limitations on the local property tax. Table II shows the trends of state and local revenues for public schools over the past 12 years.

States Are Paying Their Share

The states have clearly extended themselves to provide quality education, both in terms of per capita expenditures and as a percent of expenditures for all functions. An estimated 36 percent of all state and local expenditures is earmarked for education. Education is the single largest expenditure by state and local governments and it is usually the only one on which taxpayers vote directly. The range of state-by-state percentages is from 18 percent to 47 percent, as shown in Table III.

On the average, four percent of personal income in the states is devoted to funding public education, with a range from 2.8 percent to 7.5 percent. The actual yield of this tax effort is in average per pupil expenditures, which range from $1900 to $6400, and average teacher salaries which range from $14,000 to $34,000 (the high rate is skewed by Alaska's cost of living). State-by-state comparisons of tax effort and per pupil expenditures are shown in Table IV.

In the last five years, total expenditures for elementary and secondary education have risen from $102 billion to the current $125 billion. The proposal to eliminate the deductibility of state and local taxes would be a serious disincentive in states which are exerting massive effort to improve the quality of instruction. While the growth of expenditures is less than the inflation rate, but the states have shown a good measure of commitment to education because during that same period enrollments in the public schools dropped from 41 million pupils to 39.3 million. A substantial part of the increase in state and local support is due to efforts to reduce class size, improve teacher training, and provide better instructional materials. Also, there are very persuasive data being developed that show that the "high" tax states are also the states which contribute substantially more to the federal government than they get in return.

School Revenue Base Threatened

For education funding the problem is very direct. The decision to support or reject a millage election or a state sales tax for education is never based on "Is this deductible or not?" The voters' decision to support or reject education is based on a perception of state and local tax burden, and the loss of deductibility dramatically increases the perception of burden.

Therefore, the school revenue base would be threatened by the repeal of deductibility. Most states have constitutional requirements that their budgets be balanced, and education takes the lion's share of those budgets. The rosiest projections are for a softening of taxpayer support which would compound the difficulty of passing adequate appropriations for school support at the state level. More realistic projections would show the seeds of a taxpayer revolt.

State and local taxes have stronger support at this time than at any time in the last 14 years. It makes no sense at all to tamper with revenue sources for education that are increasingly viable. The Advisory Commission on Intergovernmental Relations study, "Changing Attitudes on Government and Taxes," shows that 35 percent of the population believes the federal income tax is the least fair, while only 26 percent object to the local property tax and 11 percent to state taxes. This represents a major change over the past decade. In 1972, only 19 percent thought that the federal income tax was the least fair, and 45 percent felt that way about the local property tax. The opinion trends are shown year by year in Table VII.

There is a strong base for education funding at the state and local level that should not be undermined by the federal government, which is the only partner in education not carrying its share of the load.

Federal Role Diminished and Federal Support Cut

Federal budgets for education have failed to keep pace with inflation in recent years. And political double-talk is clearly in season. President Reagan makes much of the public interest in improving the nation's schools. And now his tax proposals work to the detriment of education, providing a double whammy to schools when combined with Administration budget cuts.

Federal appropriations have been undercut by inflation losses and outright budget cuts, which severely limit the outreach capability of critical school programs for the disadvantaged, education of the handicapped, vocational education, and college student assistance. Fewer students are being served than in 1981.

* More than half a million students have been dropped from

eligibility and now are ineligible for Pell Grants or other programs;

- Only 45 percent of the 11 million disadvantaged children who need services under Chapter 1 receive them; in 1981 it was 55 percent.

While states have been doing their part, the federal share of elementary and secondary education funding has fallen from nine percent in 1980 to 6.2 percent. The current appropriation for federal programs for elementary, secondary, and postsecondary education is $17.9 billion, but more than $21 billion would be needed to provide services comparable to those offered in 1980. The actual losses to inflation since 1980 for major programs are shown in Table V in the appendix.

Deductibility of state and local taxes is an indirect but extremely powerful federal subsidy to state and local governments. It is a tax-efficient approach to school funding. Public education is placed in double jeopardy -- federal funding is cut while the revenue base is undermined through the loss of indirect contributions as well as public support.

Impact of the Administration Proposal on Public Education

What would happen to school financing if Congress were to deal another blow by repealing the deductibility of state and local taxes? All of the studies we have seen predict a substantial reduction in state and local spending, with education a prime target. A June, 1985, study by Merrill Lynch, Pierce, Fenner & Smith, Inc., Municipal Bonds--Perspective, warns that local political pressures to reduce income tax and property tax rates could result in severe budgetary crises. The fact that the proposal would take immediate effect in the taxable year beginning January 1, 1986, increases the likelihood that such crises will occur immediately for issuers of general obligation bonds. The study also points out that with federal revenue sharing for local governments being eliminated at the same time, many states will be under pressure to increase aid payments to their local governments. The vulnerability to fiscal crises would not be limited to "high tax" states; some states with relatively low tax burdens are heavily dependent on income taxes for general budgetary purposes. The same local political and electoral processes that have kept their tax rates low may abruptly force them even lower if taxpayers cannot deduct local taxes paid. Given the tax revolt sentiments exemplified by California's Proposition 13 and Massachusetts' Proposition 2½, the deductibility issue could become a catalyst for new tax reduction political movements in the states.

There are many estimates of the actual reduction of education expenditures by state and local governments. In a 1984 study, "Strengthening the Federal Revenue System: Implications for State and Local Taxing and Borrowing," the Advisory Commission on Intergovernmental Relations said state and local spending across the United States could be expected to fall by at least seven percent. ACIR went on to say that this was a conservative estimate; other authorities have estimated the reduction to be as high as 23 percent. The Congressional Research Service has estimated a reduction of 15 percent. Using seven and 15 percent as a base:

*The reduction would be between $4.8 billion, or $122 per child, and $10.1 billion, or $258 per child enrolled.

- *It would have the same effect on education funding as repealing virtually all federally supported elementary and secondary education programs!

Deductibility and Tax Fairness

Frequently education has been characterized as a national interest, a state responsibility, and a local commitment. In recent years we have seen more and more programs returned to the state and local level and it would seem that there is a concomitant responsibility not to destroy the funding base which is necessary to meet that reality.

Since 1913, taxes paid by individuals to state and local governments have been deductible from gross income. This provision, the most broadly used deductions in the tax code, has remained in the statute primarily because it helps to relate taxable income to the individual's ability to pay. In this sense it is a key element in a tax system based on the time-honored principle of progressivity. It is this principle of progressivity -- and basic fairness -- that generates a degree of public acceptance and cooperation that is almost unheard of in other major industrialized nations.

The Administration proposal is a tax increase that it claims would yield an estimated $39 billion - which happens to be exactly the amount by which individual income taxes were reduced in the first year of the 1981 Economic Recovery Tax Act. According to the Advisory Commission on Intergovernmental Relations, however, the revenue increase would be only $28 billion.

The Advisory Commission says the average taxpayer saved $410 in federal taxation in 1980 as a result of the deductibility of state and local taxes. State and local governments find revenue raising easier because there is greater acceptance due to the lessening of the federal tax burden. The state-by-state savings to taxpayers from the deductibility provision are shown in Table VI.

EFFECT ON EDUCATION PERSONNEL

Imposing a Tax on Health Insurance Premiums

NEA strongly supports the Administration proposal to make permanent the Congressionally mandated exclusion of employer-paid educational assistance and group legal services.

Just as strongly, we oppose the attempt to impose a tax on the first $10 worth of employer-paid health insurance premiums for individuals, and on the first $25 worth for families. This is one of the most regressive proposals in the whole package; it adds $120 to $300 of nondisposable income for every wage earner to be taxed regardless of income level.

The inclusion of a portion of employee benefits would, over time, open the door to taxing all employer-paid benefits. In our view, the longstanding policy of excluding employee benefits has advanced the health, education, and welfare of the American family just as much as the array of direct government-funded assistance to individuals and families. For middle-class Americans this provision has had a broad and deep effect.

More than 95 percent of NEA members are covered by health insurance - at least partially paid by their employers.

The exclusion of health benefits has opened up access to health care through the development of a vast system of employee group insurance, available regardless of age, sex, physical condition, or nature of employment. The contributions of employers and employees have significantly reduced pressures on charities and on social and governmental services. A tax on health premiums would not advance public policy. It would do nothing to reduce the costs of health care. It would not enhance private coverage of individuals to decrease public costs.

The Treasury claims that this provision would be easily administered, but goes on at some length to describe how the premium costs would be determined, adjusted periodically, and estimated under single and multiemployer plans. The additional employer record-keeping and compliance with nondiscrimination rules would add yet another layer of paperwork to an already considerable burden.

Public education personnel receive low salaries, as vividly shown in Table VIII in the appendix. Their benefits are important to them. Opening the bidding on taxation of benefits would be a further financial pressure against staying in the profession. Pension coverage and health benefits are two of the benefits that to some degree balance the small paycheck. For many teachers and support staff, the taxation of these benefits would be the "last straw" forcing them to leave education.

A significant longterm effect of taxing employee benefits would be the need to enact additional money measures to compensate for the relative dollar loss of employer-paid benefits. NEA believes the nation cannot now or in the future afford the loss of those benefits. The tax law has encouraged pension coverage broadly among lower- and middle-income workers, affording families a type of savings plan that would be difficult to maintain on individual initiative. Educational assistance has helped the unemployed, the underemployed, and lower wage earners to help themselves. Group life and accident insurance provide enormously valuable protection to families, and such programs are for most workers an irreplaceable supplement to private insurance and Social Security coverage. Tax law which provides these significant benefits to society must be preserved.

Retirement Savings for Public Employees

Under current law, I.R.S. Code Sec. 403(b), employees of public schools and certain nonprofit public service organizations are allowed to defer paying taxes on a portion of their income. This law, in effect since the late 1950's, is an enormous incentive for talented people to work for schools rather than in the private sector. It enables public schools and other nonprofit organizations to more closely compete with the private sector's higher salaries and better benefits. It has been segregated from other tax-deferred plans such as IRA's, 401(k), and Keogh plans in that it allows for access to funds without penalty prior to age 59½. The Administration proposal would change the dollar amount that school employees could defer from income to a maximum of 16 2/3 percent. Also, the proposal would eliminate partial withdrawls prior to age 59½ without imposing a severe 20 percent tax penalty.

Most people working in education do not earn enough to change to more aggressive vehicles, and therefore see their tax-deferred annuities as their primary financial planning tool and often their only means for buying a home or sending children to college, as well as supplementing their inadequate public retirement plans. Also, the inability of education personnel to make a withdrawal without severe penalties or to borrow against their funds would prevent them from accessing the only funds they may have set aside for the future. The Administration proposal unfairly changes the rules in the middle of the game for such employees, and we strongly urge that Congress retain the current 403(b) provisions intact.

Employer Matching Contribution Rules

Current law allows employees to elect to defer the receipt of cash compensation and have the deferred amount paid as an elective contribution to a qualified profit-sharing or stock bonus plan. The Administration proposal would not permit tax-exempt organizations and state or local governments to enter into such arrangements on the grounds that such entities already have pension plans and tax-sheltered annuities. The 401(k) cash or defferred arrangement (CODA) plans allow a great deal of flexibility -- employees need not make elective contributions unless their personal financial circumstances permit. Employees may invest up to 20 percent of salary in these plans, employers may contribute an additional 15 percent, and employees may borrow against their savings. The CODA has greater rollover flexibility for both the employee and the employee's widow or widower. Lump sum distribution can be averaged over ten years, as opposed to only four years under other plans. These features are not available in other annuity plans available to our members, and we urge that they continue to be available to public employees.

Maintaining a Strong Family Policy -- The Two-Earner Deduction, the Child Care Credit, and Adoption Expense Deduction

The tax bill of 1981 included a significant provision for our members -- the lessening of the "marriage tax penalty." The Reagan plan proposes to repeal this provision. This provision reduced the marginal tax rate by ten percent for second earners. The Administration states that reductions in the tax rate itself and in the number of steps makes this provision unnecessary since very few families will be pushed into the next income bracket by the spouse's income.

We believe that political philosophy, not tax policy, drives this proposal The sweep of the 1981 bill was broad and worked to preserve the financial integrity of families with two working spouses. It was reflective of the American family today. A few statistics make the case for retention of a deduction which was designed to reduce the tax penalty for two married wage-earners -- a penalty not imposed on single wage-earners.

* Approximately 73 percent of American households consist of married couples with or without children ("Social Stratification in the U.S." by Stephen Rose, based on U.S. Census Bureau data).
* More than 52 percent of all married women now work outside the home. But these women earn, on average, only 60 cents for every dollar men earn ("Unfinished Business: Adequacy and Equity for

Women in the Social Security System," published by the Save Our Security Coalition, Washington, D.C.)

The disparity of income levels between men and women clearly indicates the importance of assuring that the second income in a family is not penalized by the tax code. The marketplace consistently underrates traditionally female work -- three out of five working women make less than $10,000 per year. While only 12 percent of fully employed men make less than $7,000 per year, 33 percent of women fall into this category. In 1984, 52 percent of mothers with children under six years of age were employed; 55 percent of mothers with school-age children were employed.

Deliberately or not, the Reagan plan introduces a sweeping new social policy affecting millions of taxpayers, both men and women. Where the current tax code offers limited assistance to working couples, the proposal would again penalize those couples or encourage the lower-earning spouse -- generally the woman -- to stay at home.

The replacement of the child care credit with a deduction is another manifestation of this policy switch. The Administration's proposal is based on a premise similar to that for the repeal of the two-earner deduction: lower tax rates. What the Administration chooses to ignore is that the child care tax credit is critically needed, and -- in our view, and that of a wide range of business, labor, and other groups, should be expanded. We support efforts of the Congressional Caucus on Women's Issues in this regard.

Current law provides a graduated scale of tax credits based upon income levels and should be retained. Taken together, these two proposals, to decrease support for child care and to repeal the two-earner deduction, sound suspiciously like a 1980's version of "barefoot and pregnant."

In addition, current law allows a deduction for qualified adoption expenses paid or incurred during the taxable year, including adoption fees, court costs, and attorney's fees. The Administration proposes to repeal this deduction because of the availability of federal support for children with special needs, as defined by the Social Security Act. We believe the adoption deduction should be broadly available to maximize the opportunity for children to be brought up in a family setting, by parents who will give them love and care as if they were their own. Existing federal programs are useful, but they are no substitute for the initiative of childless couples and individuals who can offer the abundant riches of family life to children who would otherwise be shunted from orphanage to foster home and back again. The tax code can and should encourage, rather than discourage, this important humanitarian practice.

The Elderly Are at Risk with the Tax on Social Security Benefits

One of the undesirable features of the 1983 Social Security Amendments was the imposition of income taxes on a portion of benefits for retirees with incomes over $25,000 -- or $32,500 for married couples. In our view, this tax represents a tax on a tax; the Social Security benefits that retirees receive is an earned benefit, paid for by payroll taxes for which the wage earner is liable. Not every beneficiary gets back all or more than he or she has paid in payroll taxes, and our members have been especially critical of this provision in the 1983 statute, which has nothing to do with restoring the solvency of the Old Age and Survivors'

Insurance trust fund. The taxation of Social Security benefits is a thinly disguised reduction of benefits and is tantamount to a means test that breaks the social compact that Social Security is intended to be.

As several members of the National Commission on Social Security Reform have pointed out, the requirement that Social Security beneficiaries include interest from tax-exempt bonds on their returns is a bizarre departure from previous tax law. If such interest is not to be included in taxable income, there is no justification for having to report it.

The Administration plan would make no change in the 1983 law. We urge Congress to repeal the taxation of Social Security benefits to restore confidence in the system and to eliminate the requirement for reporting tax-exempt income.

Educational Travel Deduction Benefits Instruction

For many years, teachers have used educational travel as an effective way to upgrade their teaching skills. Their personal experiences in a variety of political, cultural, and literary centers of the world have contributed substantially to the improvement of instruction in the classroom. The Administration seeks to disallow deductions for educational travel purely on the grounds that present limitations fail to distinguish adequately between costs incurred for business purposes and costs reflecting personal consumption.

Current law permits the deduction of travel expenses only if the major portion of the activities during the period of travel is of a nature that directly maintains or improves skills required in the taxpayer's employment or business, and case law differentiates clearly between deductible and nondeductible expenses. We think this is fair. The President's proposal would simply deny deduction of education travel expenses because it is inconvenient for IRS to identify abuses. Events during the tax season of 1985 suggest that, if the convenience of IRS is a criterion for decisionmaking about the tax code, the whole system of taxation should be scrapped!

More clarity in the regulations would be preferable to an outright cancellation of the deduction, which would make it impossible for many, if not most, teachers to further their education and training in this way. We urge that this proposal be rejected.

Charitable Contributions Deduction

Under present law, taxpayers who do not itemize deductions are allowed a deduction for charitable contributions. The $300 limitation is to be removed in 1986 and 100 percent of such contributions are to be deductible. This incentive to itemizers for charitable giving can be of great benefit to educational, charitable, religious, and other tax-exempt organizations. The Administration believes there is no way to determine whether charitable giving has been encouraged by this tax provision, but the full benefit of current law will not be available until 1986 -- the year in which the deduction expires. In our view, the needs of education institutions and charitable organizations are so great in a time of reduced federal spending on social programs that the elimination of this deduction during its first full year of implementation is unwise -- and totally inconsistent with the Administration's own emphasis on voluntary, private-sector support of social programs.

Poor Social Policy -- Repealing Political Contributions

The tax credit for political campaign contributions is designed to encourage individuals to contribute to the cost of the political process. It opens up a form of participation in our nation's political life that can act as a foil to the effectiveness of well-funded special interests and wealthy individuals. The Administration cites administrative and compliance problems, but we see no reason to remove this incentive to individual participation as long as adequate record keeping is required.

Similarly, the Administration proposes to abolish the Presidential campaign check-off. According to the Treasury, one fourth of all taxpayers use this privilege, which again offers individual taxpayers at least a small share in the most important political process in the nation, and its use should be encouraged rather than denied. In addition it is the base for federal financing of Presidential elections. A decision to change such an important electoral process should be the subject of extensive research -- not a footnote in the tax debate.

CONCLUSION

The National Education Association supports tax reform and believes that the tax code should be progressive and support the independence of the family. It should strike a fair balance between individual and family taxpayers as well as corporate taxpayers. For acceptability to the public, the tax code should be based upon a fair and progressive distribution scheme which does not unduly burden the poor or the middle class. Finally, the tax code should be simple for taxpayers and cost-effective to administer. On many of these criteria the Reagan plan succeeds. In other critical areas it fails; we have identified them within our testimony. For the well-being of public education and the men and women who work in America's schools we ask that you give particular attention to assuring that the state and local tax deduction continues and that employer-provided benefits remain untaxed.

APPENDIX

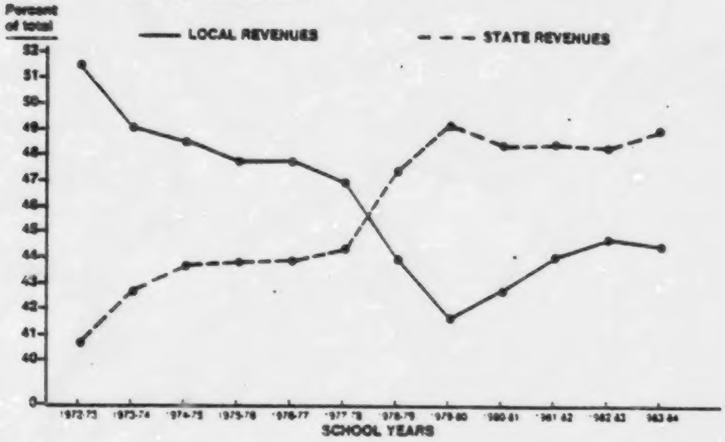
Table I. Funding Patterns for Public Schools

REGION AND STATE	REVENUE RECEIPTS BY SOURCE (IN THOUSANDS)				PERCENT OF REVENUE RECEIPTS BY SOURCE			NONREVENUE RECEIPTS (IN THOUSANDS)	TOTAL RECEIPTS (COLS. 5 AND 9) (IN THOUSANDS)
	FEDERAL	STATE	LOCAL AND OTHER	TOTAL	FEDERAL	STATE	LOCAL AND OTHER		
1	2	3	4	5	6	7	8	9	10
50 STATES AND D.C.	$8,585,605	$67,188,982	$61,998,030	$137,572,617	6.2	49.0	44.8	$3,992,297	$141,564,914
NEW ENGLAND	401,066	2,966,617	4,153,083	7,520,766	5.3	39.4	55.2	29,066	7,549,828
CONNECTICUT	105,720	851,178	1,173,215	2,130,113	5.0	40.0	55.1	400	2,130,513
MAINE	47,525	318,563	258,652	624,740	7.6	51.0	41.4	15,000	639,740
MASSACHUSETTS	190,510	1,459,831	1,782,894	3,433,235	5.5	42.5	51.9	6,000	3,439,235
NEW HAMPSHIRE	15,667	39,567	437,966	493,200	3.2	8.0	88.8	1,364	494,564
RHODE ISLAND	20,761	186,196	293,336	500,293	4.1	36.8	59.0	0	500,293
VERMONT	20,921	113,262	205,000	339,183	6.2	33.4	60.4	6,300	345,483
MIDEAST	1,166,409	12,175,271	15,291,950	28,611,630	4.0	42.6	53.4	1,236,426	29,848,056
DELAWARE	30,800	272,660	89,200	392,660	7.8	69.4	22.7	10,600	403,260
DIST. OF COLUMBIA	43,529	...	340,652	384,181	11.3	...	88.7	...	384,181
MARYLAND	152,223	1,084,381	1,446,420	2,683,004	5.7	40.4	53.9	3,561	2,686,565
NEW JERSEY	196,600	2,288,900	3,236,900	5,722,400	3.4	40.0	56.6	87,100	5,809,500
NEW YORK	501,617	5,422,000	6,659,708	12,583,325	4.0	43.1	52.9	566,675	13,150,000
PENNSYLVANIA	221,840	3,107,350	3,516,870	6,846,060	3.2	45.4	51.4	568,490	7,414,550
SOUTHEAST	2,489,784	15,175,380	9,354,247	27,019,411	9.2	56.2	34.6	743,159	27,762,570
ALABAMA	195,000	1,182,119	255,000	1,632,119	11.9	72.4	15.6	80,000	1,712,119
ARKANSAS	117,533	634,853	320,000	1,072,386	11.0	59.2	29.8	7,808	1,080,194
FLORIDA	412,572	3,061,069	2,251,450	5,725,091	7.2	53.5	39.3	78,000	5,803,091
GEORGIA	269,265	1,430,151	1,144,580	2,843,996	9.5	50.3	40.2	51,869	2,895,865
KENTUCKY	171,000	1,160,500	359,000	1,690,500	10.1	68.6	21.2	75,000	1,765,500
LOUISIANA	226,300	1,254,300	866,600	2,347,200	9.6	53.4	36.9	78,000	2,425,200
MISSISSIPPI	182,015	578,926	260,126	1,021,067	17.8	56.7	25.5	27,682	1,048,749
NORTH CAROLINA	288,100	1,713,600	786,200	2,787,900	10.3	61.5	28.2	10,500	2,798,400
SOUTH CAROLINA	120,633	1,095,365	527,740	1,743,738	6.9	62.8	30.3	120,000	1,863,738
TENNESSEE	193,310	976,177	788,700	1,958,187	9.9	49.9	40.3	132,500	2,090,687
VIRGINIA	210,542	1,364,763	1,484,673	3,059,978	6.9	44.6	48.5	80,000	3,139,978
WEST VIRGINIA	103,516	723,557	310,176	1,137,249	9.1	63.6	27.3	1,800	1,139,049
GREAT LAKES	1,231,771	9,736,556	13,372,164	24,340,491	5.1	40.0	54.9	712,915	25,053,406
ILLINOIS	441,192	2,488,443	3,684,668	6,614,303	6.7	37.6	55.7	156,731	6,771,034
INDIANA	120,000	1,524,000	1,211,000	2,855,000	4.2	53.4	42.4	73,500	2,928,500
MICHIGAN	254,048	2,034,386	3,721,310	6,009,744	4.2	33.9	61.9	57,000	6,066,744
OHIO	310,000	2,600,000	3,190,000	6,100,000	5.1	42.6	52.3	400,000	6,500,000
WISCONSIN	106,531	1,089,727	1,565,186	2,761,444	3.9	39.5	56.7	25,684	2,787,128
PLAINS	520,137	4,147,928	5,005,222	9,673,287	5.4	42.9	51.7	171,313	9,844,600
IOWA	92,069	708,265	886,982	1,687,316	5.5	42.0	52.6	35,775	1,723,091
KANSAS	68,900	681,319	761,478	1,511,697	4.6	45.1	50.4	24,546	1,536,243
MINNESOTA	106,000	1,347,100	1,140,220	2,593,320	4.1	51.9	44.0	43,000	2,636,320
MISSOURI	144,666	871,342	1,323,446	2,339,454	6.2	37.2	56.6	45,192	2,384,646
NEBRASKA	45,000	232,000	548,000	825,000	5.5	28.1	66.4	15,000	840,000
NORTH DAKOTA	25,000	209,500	117,500	352,000	7.1	59.5	33.4	7,000	359,000
SOUTH DAKOTA	38,500	98,000	228,000	364,500	10.6	26.9	62.6	800	365,300
SOUTHWEST	1,217,222	7,435,031	6,118,698	14,770,951	8.2	50.3	41.4	777,423	15,548,374
ARIZONA	160,000	801,000	568,000	1,529,000	10.5	52.4	37.1	0	1,529,000
NEW MEXICO	98,637	691,250	103,288	893,175	11.0	77.4	11.6	17,380	910,555
OKLAHOMA	146,000	1,220,000	620,000	1,986,000	7.4	61.4	31.2	110,000	2,096,000
TEXAS	812,585	4,722,781	4,827,410	10,362,776	7.8	45.6	46.6	650,043	11,012,819
ROCKY MOUNTAINS	249,900	2,136,886	2,368,379	4,751,165	5.2	45.0	49.8	176,906	4,928,071
COLORADO	80,000	819,596	1,139,262	2,038,856	3.9	40.2	55.9	45,000	2,083,856
IDAHO	34,000	325,000	143,000	502,000	6.8	64.7	28.5	10,000	512,000
MONTANA	55,500	276,973	283,217	615,690	9.0	45.0	46.0	19,710	635,400
UTAH	54,400	545,319	402,900	1,002,619	5.4	54.4	40.2	52,196	1,054,815
WYOMING	22,000	170,000	400,000	592,000	3.7	28.7	67.6	50,000	642,000
FAR WEST	1,335,318	13,615,715	5,933,885	20,884,918	6.4	65.2	28.4	145,091	21,030,009
ALASKA	20,149	501,748	161,518	683,415	2.9	73.4	23.6	23,527	706,942
CALIFORNIA	1,011,350	9,937,825	3,866,000	14,815,175	6.8	67.1	26.1	70,000	14,885,175
HAWAII	51,800	527,000	1,300	580,100	8.9	90.8	.3	0	580,100
NEVADA	18,400	182,000	260,000	460,400	4.0	39.5	56.5	8,400	468,800
OREGON	84,337	499,180	1,136,483	1,720,000	4.9	29.0	66.1	3,000	1,723,000
WASHINGTON	149,482	1,967,962	508,384	2,625,828	5.7	74.9	19.4	40,164	2,665,992

Souce: Estimates of School Statistics, 1984-85
NEA Research

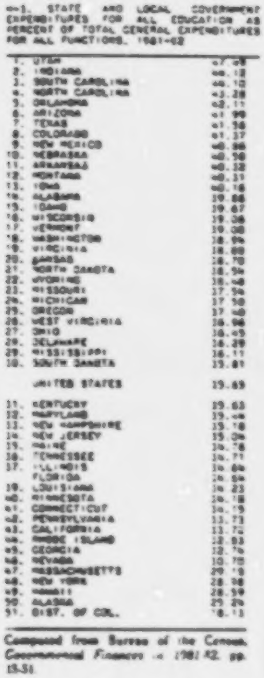
Table II. State and Local School Revenues, 1972-1984

State and Local Revenue Receipts for Public Schools
1972-73 to 1983-84



Source: Property Taxation
NEA Research, 1985

Table III. State Education Expenditures as a Percent of All Expenditures



H-1. STATE AND LOCAL GOVERNMENT EXPENDITURES FOR ALL EDUCATION AS PERCENT OF TOTAL GENERAL EXPENDITURES FOR ALL FUNCTIONS, 1981-82

1.	UTAH	47.48
2.	INDIANA	44.12
3.	SOUTH CAROLINA	44.10
4.	NORTH CAROLINA	43.28
5.	OKLAHOMA	42.11
6.	ARIZONA	41.90
7.	TEXAS	41.56
8.	COLORADO	41.37
9.	NEW MEXICO	40.86
10.	NEBRASKA	40.50
11.	ARKANSAS	40.32
12.	MONTANA	40.31
13.	IOWA	40.16
14.	ALABAMA	39.86
15.	IDAHO	39.67
16.	WISCONSIN	39.36
17.	VERMONT	39.08
18.	WASHINGTON	38.94
19.	VIRGINIA	38.88
20.	KANSAS	38.70
21.	NORTH DAKOTA	38.54
22.	WYOMING	38.48
23.	MISSOURI	37.54
24.	MICHIGAN	37.50
25.	OREGON	37.40
26.	WEST VIRGINIA	36.96
27.	OHIO	36.45
28.	DELAWARE	36.29
29.	MISSISSIPPI	36.11
30.	SOUTH DAKOTA	35.81
	UNITED STATES	35.69
31.	KENTUCKY	35.63
32.	MARYLAND	35.48
33.	NEW HAMPSHIRE	35.16
34.	NEW JERSEY	35.04
35.	MAINE	34.76
36.	TENNESSEE	34.71
37.	ILLINOIS	34.64
	FLORIDA	34.64
39.	LOUISIANA	34.23
40.	MINNESOTA	34.18
41.	CONNECTICUT	34.15
42.	PENNSYLVANIA	33.73
43.	CALIFORNIA	33.72
44.	RHODE ISLAND	32.93
45.	GEORGIA	32.76
46.	NEVADA	30.75
47.	MASSACHUSETTS	29.19
48.	NEW YORK	28.98
49.	HAWAII	28.59
50.	ALASKA	25.24
51.	DIST. OF COL.	18.13

Compiled from Bureau of the Census, *Governmental Finances in 1981-82*, pp. 15-31.

Source: Rankings of the States, 1984
NEA Research

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Table IV. State Tax Effort, Per Pupil Expenditures

F-4. STATE AND LOCAL REVENUE RECEIPTS FOR PUBLIC SCHOOLS IN 1981-82 AS PERCENT OF PERSONAL INCOME IN 1982

1.	ALASKA	7.57
2.	WYOMING	6.88
3.	MONTANA	5.96
4.	UTAH	5.48
5.	NEW MEXICO	5.46
6.	MICHIGAN	5.10
7.	OREGON	5.09
8.	VERMONT	5.00
9.	WEST VIRGINIA	4.96
10.	MINNESOTA	4.79
11.	NEW YORK	4.62
12.	IOWA	4.60
13.	MAINE	4.57
14.	INDIANA	4.55
15.	NEW JERSEY	4.52
16.	IDAHO	4.51
	WISCONSIN	4.51
18.	SOUTH DAKOTA	4.33
19.	PENNSYLVANIA	4.32
20.	KANSAS	4.29
21.	ARIZONA	4.28
22.	OKLAHOMA	4.27
23.	DELAWARE	4.23
24.	MASSACHUSETTS	4.19
25.	WASHINGTON	4.18
26.	NORTH DAKOTA	4.17
27.	COLORADO	4.16
28.	TEXAS	4.12
29.	MARYLAND	4.11
	UNITED STATES	4.10
30.	RHODE ISLAND	4.05
31.	LOUISIANA	4.04
32.	SOUTH CAROLINA	4.02
33.	NEW HAMPSHIRE	3.97
34.	GEORGIA	3.95
35.	ARKANSAS	3.84
	NORTH CAROLINA	3.84
37.	OHIO	3.83
38.	ILLINOIS	3.82
39.	NEBRASKA	3.78
40.	HAWAII	3.72
41.	VIRGINIA	3.69
42.	NEVADA	3.68
	CONNECTICUT	3.68
44.	KENTUCKY	3.65
45.	MISSOURI	3.60
46.	MISSISSIPPI	3.56
47.	TENNESSEE	3.48
	CALIFORNIA	3.48
49.	FLORIDA	3.36
50.	ALABAMA	2.79
	DIST. OF COL.	NA

Computed from Bureau of Economic Analysis, *Survey of Current Business*, August 1983, p. 50; and NEA Research, *Estimates* data bank.

H-9. ESTIMATED CURRENT EXPENDITURES FOR PUBLIC ELEMENTARY AND SECONDARY SCHOOLS PER PUPIL IN AVERAGE DAILY ATTENDANCE, 1982-83 (REVISED)

1.	ALASKA	$6,383
2.	NEW YORK	4,434
3.	NEW JERSEY	4,428
4.	DIST. OF COL.	4,083
5.	WYOMING	4,043
6.	CONNECTICUT	3,666
7.	OREGON	3,604
8.	DELAWARE	3,524
9.	MARYLAND	3,488
10.	MONTANA	3,442
11.	MASSACHUSETTS	3,406
12.	RHODE ISLAND	3,389
13.	PENNSYLVANIA	3,385
14.	WISCONSIN	3,380
15.	HAWAII	3,347
16.	MICHIGAN	3,178
17.	MINNESOTA	3,136
18.	VERMONT	3,102
19.	KANSAS	3,093
20.	IOWA	3,055
21.	ILLINOIS	3,018
22.	COLORADO	2,961
	UNITED STATES	2,960
23.	FLORIDA	2,923
24.	OKLAHOMA	2,902
25.	WASHINGTON	2,878
26.	NEW MEXICO	2,843
27.	NORTH DAKOTA	2,836
28.	TEXAS	2,820
29.	LOUISIANA	2,780
30.	VIRGINIA	2,737
31.	CALIFORNIA	2,735
32.	NEBRASKA	2,708
33.	NEVADA	2,698
34.	OHIO	2,696
35.	MAINE	2,624
36.	NEW HAMPSHIRE	2,561
37.	INDIANA	2,532
38.	ARIZONA	2,512
39.	SOUTH DAKOTA	2,472
40.	WEST VIRGINIA	2,465
41.	MISSOURI	2,396
42.	KENTUCKY	2,368
43.	NORTH CAROLINA	2,265
44.	GEORGIA	2,155
45.	IDAHO	2,106
46.	UTAH	2,080
	SOUTH CAROLINA	2,080
48.	TENNESSEE	2,061
49.	ALABAMA	2,019
50.	ARKANSAS	1,998
51.	MISSISSIPPI	1,895

Computed from NEA Research, *Estimates* data bank.

Source: Rankings of the States, 1984
NEA Research

Table V. Diminution of Federal Support of Education, 1980-1985

Reagan Budget FY86 vs. Inflation Adjustment

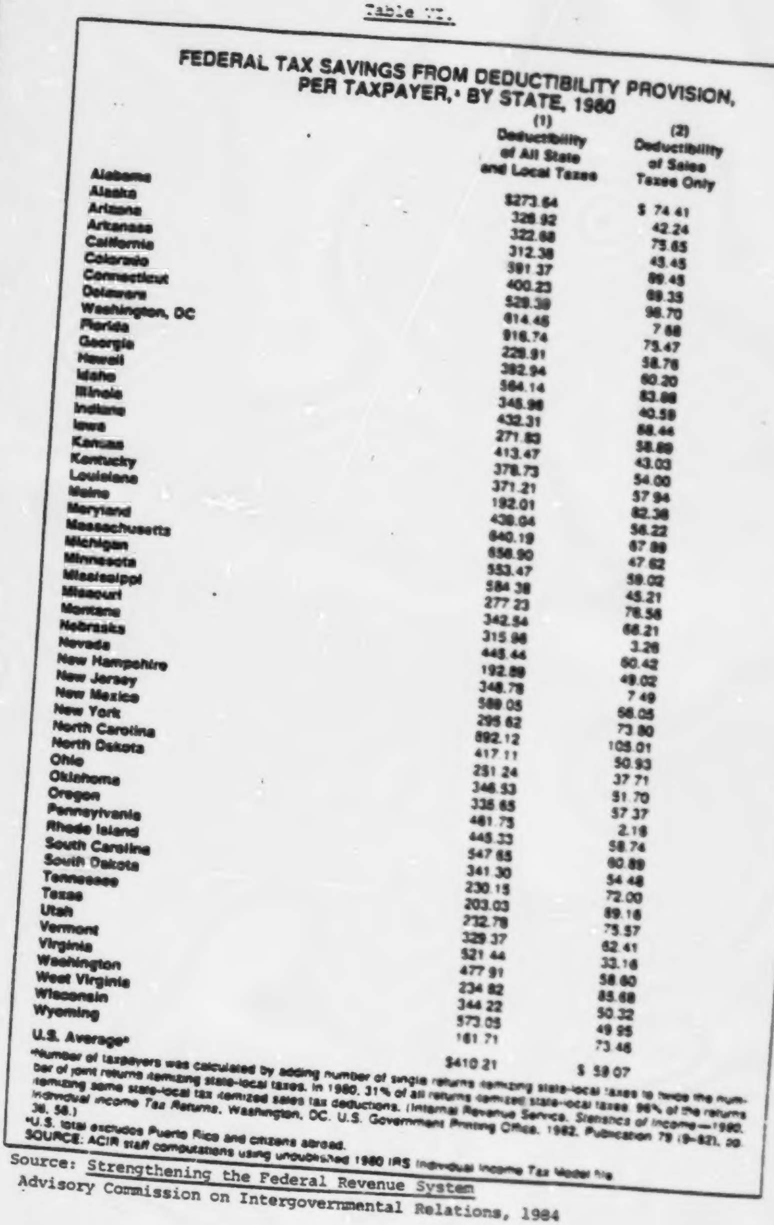
National Totals
Appropriations, Thousands of Dollars

Program	Appropriations FY80 (School Year '80-'81)	FY80 Adjusted For Inflation (School Year '86-'87) Since 1980	Reagan Budget FY86 (School Year '86-'87)	Difference Reagan Budget FY86 vs. Inflation Adjustment
Education Department	14299100	21870256	15512700	-6357556
SELECTED FEDERAL EDUCATION PROGRAMS:				
ECIA Chapter I (ESEA Title I Basic Grants)	3221099	4893409	3646615	-1246794
State Block Grant (ECIA Chapter II)	802581	1220411	531909	-688502
Impact Aid (not forward funded)	825000	1251483	541000	-710483
Education for the Handicapped	1049825	1593326	1306100	-287226
Vocational Education	801841	1216171	738462	-477709
Adult Education	100000	151006	100000	-51006
Bilingual Education	171763	260885	142951	-117934
New Math and Science Bill	0	0	100000	100000
Pell Grants	2530000	3839606	2880000	-959606
Supplemental Educational Opportunity Grants	370000	561979	0	-561979
College Work Study	550000	835375	850000	14625

NOTE: Figures for FY86 Adjusted for Inflation represent amounts required to maintain FY 1980 funding levels after accountin for inflation. Inflation (CPIU) is measured for the period of a Federal Fiscal Year (October 1 through September 30) Inflation estimates for 1985 are derived from projections by Data Resources, Inc.

Source: Fiscal Planning Services, Inc.
Washington, DC

Table VI.



FEDERAL TAX SAVINGS FROM DEDUCTIBILITY PROVISION, PER TAXPAYER,[a] BY STATE, 1980

	(1) Deductibility of All State and Local Taxes	(2) Deductibility of Sales Taxes Only
Alabama	$273.64	$ 74.41
Alaska	328.92	42.24
Arizona	322.68	75.65
Arkansas	312.38	45.45
California	391.37	89.45
Colorado	400.23	69.35
Connecticut	529.39	98.70
Delaware	614.45	7.88
Washington, DC	916.74	75.47
Florida	228.91	58.76
Georgia	382.94	60.20
Hawaii	564.14	83.88
Idaho	345.98	40.59
Illinois	432.31	68.44
Indiana	271.83	58.89
Iowa	413.47	43.03
Kansas	378.73	54.00
Kentucky	371.21	57.94
Louisiana	192.01	82.38
Maine	438.04	56.22
Maryland	640.19	67.88
Massachusetts	656.90	47.62
Michigan	553.47	59.02
Minnesota	584.38	45.21
Mississippi	277.23	78.56
Missouri	342.54	66.21
Montana	315.98	3.28
Nebraska	445.44	60.42
Nevada	192.89	49.02
New Hampshire	348.78	7.49
New Jersey	589.05	56.05
New Mexico	295.62	73.80
New York	892.12	105.01
North Carolina	417.11	50.93
North Dakota	251.24	37.71
Ohio	346.53	51.70
Oklahoma	335.65	57.37
Oregon	461.75	2.18
Pennsylvania	445.33	58.74
Rhode Island	547.65	60.89
South Carolina	341.30	54.48
South Dakota	230.15	72.00
Tennessee	203.03	89.16
Texas	232.78	75.57
Utah	329.37	62.41
Vermont	521.44	33.16
Virginia	477.91	58.60
Washington	234.82	85.68
West Virginia	344.22	50.32
Wisconsin	573.05	49.95
Wyoming	161.71	73.48
U.S. Average[b]	$410.21	$ 58.07

[a] Number of taxpayers was calculated by adding number of single returns itemizing state-local taxes to twice the number of joint returns itemizing state-local taxes. In 1980, 31% of all returns itemized state-local taxes. 96% of the returns itemizing some state-local tax itemized sales tax deductions. (Internal Revenue Service, *Statistics of Income—1980, Individual Income Tax Returns*, Washington, DC. U.S. Government Printing Office, 1982, Publication 79 (9-82), pp. 38, 58.)

[b] U.S. total excludes Puerto Rico and citizens abroad.

SOURCE: ACIR staff computations using unpublished 1980 IRS Individual Income Tax Model file.

Source: Strengthening the Federal Revenue System
Advisory Commission on Intergovernmental Relations, 1984

Table VII. Public Opinion on Taxation

Which Do You Think is the Worst Tax—That is, the Least Fair?

	May 1983	May 1982	Sept. 1981	May 1980	May 1979	May 1978	May 1977	May 1975	April 1974	May 1973	March 1972
Federal Income Tax	35	36	36	36	37	30	28	28	30	30	19
State Income Tax	11	11	9	10	8	11	11	11	10	10	13
State Sales Tax	13	14	14	19	15	18	17	23	20	20	13
Local Property Tax	26	30	33	25	27	32	33	29	28	31	45
Don't Know	15	9	9	10	13	10	11	10	14	11	11

SOURCE: *U.S. Advisory Commission on Intergovernmental Relations. 1983 Changing Attitudes on Governments and Taxes.* Washington, DC 20575.

Table VIII

Average Salaries of Instructional Staff, 1984-85
Showing Percent Increases over 1983-84
and Purchasing Power in 1967 Dollars

	State	Average Salary of Instructional Staff	Percent of Increase Over 1983-84	Purchasing Power in 1967 Dollars
1.	Alabama	20,834	14.3	6,282
2.	Alaska	41.000	5.1	12,357
3.	Arizona	25,838	8.0	7,268
4.	Arkansas	19,575	11.8	5,885
5.	California	27,580	5.9	8,175
5.	Colorado	25,382	5.1	7,602
7.	Connecticut	25,650	8.4	7,622
8.	Delaware	24,134	11.3	7,243
9.	District	29,770	3.5	8,897
10	Florida	22,480	8.0	6,546
11.	Georgia	21,407	10.0	6,371
12.	Hawaii	25,295	1.1	7,656
13.	Idaho	20,420	9.5	6,124
14.	Illinois	26,703	6.8	8,029
15.	Indiana	23,882	7.2	7,177
16.	Iowa	21,686	3.9	6,507
17.	Kansas	22,564	9.5	6,592
18.	Kentucky	21,300	2.2	6,248
19.	Louisiana	20,110	7.0	6,121
20.	Maine	18,935	5.8	5,698
21.	Maryland	26,782	7.3	8,039
22.	Massachusetts	28,000	5.0	7,495
23.	Michigan	29,610	5.0	8,828
24.	Minnesota	26,500	6.4	8,057
25.	Mississippi	16,519	1.0	4,965
26.	Missouri	21,362	5.9	6,357
27.	Montana	22,440	4.9	6,747
28.	Nebraska	21,529	7.3	6,265
29.	Nevada	23,550	.7	7,000
30.	New Hampshire	19,276	6.9	5,775
31.	New Jersey	26,310	8.0	7,810
32.	New Mexico	23,240	7.3	6,859
33.	New York	29,700	6.2	9,015
34.	North Carolina	21,357	13.0	6,432
35.	North Dakota	20,480	3.3	6,186
36.	Ohio	23,682	6.8	7,068
37.	Oklahoma	19,520	1.9	5,884
38.	Oregon	25,974	7.5	7,737
39.	Pennsylvania	25,113	7.6	7,596
40.	Rhode Island	25,253	8.1	8,512
41.	South Carolina	20,770	13.9	6,155
42.	South Dakota	18,048	5.3	5,395
43.	Tennessee	20,450	12.1	6,242
44.	Texas	23,500	12.0	7,025
45.	Utah	24,475	6.5	6,623
46.	Vermont	19,640	8.0	5,910
47.	Virginia	22,400	9.5	6,694
48.	Washington	26,727	5.1	7,961
49.	West Virginia	20,451	11.9	6,081
50.	Wisconsin	25,160	8.6	7,703
51.	Wyoming	26,935	6.0	8,302

Source: Estimates of School Statistics, 1984-85
NEA Research

STATEMENT BY ALBERT SHANKER, PRESIDENT, AMERICAN FEDERATION OF TEACHERS, WASHINGTON, DC, ACCOMPANIED BY GREG HUMPHREY, ASSISTANT FOR GOVERNMENT AFFAIRS, AFT

Mr. SHANKER. Thank you very much.

Mr. Chairman, members of the committee, I have with me Greg Humphrey, my assistant for government affairs. We have submitted a written statement, I will spend the time that I have on the issue of the loss of deductibility of State and local taxes.

We have spent 2 years in the United States stressing the importance of improving our educational system through a movement which was largely spurred by a report called "A Nation At Risk," by a Commission appointed by the Secretary of Education was largely popularized through the President's Bully Pulpit, has helped cause improvements and changes in public education throughout the country. Ironically this tax proposal by President Reagan, will have a devastating impact on education is being made at the same time we are struggling to improve our schools.

All of the reports, almost 30 of them including "A Nation At Risk," have cited that while more money alone was not the answer, that there ought to be an exchange of sorts by which the business community and the political community would invest more money in schools if, and only if, there were real and substantive changes made within the educational community. This indeed is what has been going on, and it has been going on at the very same time that the Federal Government has been reducing its support for State and local government. In almost 16,000 localities throughout the country, taxpayers have raised taxes and have increased their support for public education.

Now, at the same time that that effort is going on, to have the Federal Government adopt a tax policy which undermines and undercuts the ability of State and local government either to raise taxes or even to maintain the taxes they now have, will work against the success of this very desirable movement which has been taking place over the last few years.

Now, there is no doubt that people look at the taxes they pay. I don't think that point need any elaboration. I think they also know that when they pay State and local taxes they are quite aware of the fact that some of that lost is recovered through deductibility. Economists have a word for it, basically they know that when they are paying their school taxes they are paying 72 cents for every dollar in taxes. Should this change go through, they will realize that they are not paying 72 cents anymore; they are paying the full dollar. That represents a 40-percent increase in what it will cost taxpayers to maintain the schools in this country. When you have a 40-percent increase in the price of something, there are ways of resisting. In the private sector, you might not buy a product at all, or you might not buy as much of it, or you might seek a cheaper product. In the public sector it will manifest itself in efforts to either reduce existing taxes or in resistence to necessary tax increases. I point out the economics of it in the written presentation.

I would like to underscore a particular contradiction in the administration's program in this respect. We support the notion that charitable contributions ought to be tax-deductible, and we have supported previous moves to make it possible for those who don't itemize to take a charitable deduction. The art thinks the role that nonprofit charitable institutions in our society plays is very important. But isn't it strange that if I were to contribute money to a number of private charities which run private schools or run libraries or health facilities, and which privately perform exactly the same services that are performed publicly, that my private contributions would be tax deductible but that money taken from me democratically, by a vote of a legislature or indeed by a referendum in my community, would not be a deductible?

I would like finally to address the question of whether this is a question of favored States and unfavored States. I would point out that in the last few years a number of States have found that, in order to attract industry and in order to pormote economic development, they had to raise taxes. Texas had a substantial increase on the advice of H. Ross Perot, who headed a Governor's Commission on Excellence in Education. Lamar Alexander in Tennessee decided to impose a 1 penny increase in the sales tax for education. Arkansas, Mississippi also have increased their taxes. And if we were to move in a direction indicated by the administration, we would be preventing those States that have underdeveloped public structures, from the point of view of attracting industry and economic development, we would make it more difficult for them to catch up in some of the public services which they now lack.

Thank you.

The CHAIRMAN. Thank you.

Mr. Lucy.

[Mr. Shanker's written testimony follows:]

STATEMENT OF ALBERT SHANKER, PRESIDENT
AMERICAN FEDERATION OF TEACHERS, AFL-CIO
TO THE SENATE COMMITTEE ON FINANCE
ON TAX SIMPLIFICATION LEGISLATION

July 28, 1985

Mr. Chairman, Members of the Committee:

Thank you on behalf of the 610,000 members of the American Federation of Teachers for this opportunity to testify. I will use this occasion to call the Committee's attention to some of the implications President Reagan's tax plan has for public education.

In the opinion of the AFT, the President's tax plan as presented to the Congress will do more harm than good. As we view the elements of the new proposed tax structure, we find President Reagan seeks a continuation of most of the tax preferences enacted in 1981. In addition, the 1985 tax plan would have the effect of severely hamstringing education reform efforts by eliminating the deductibility of taxes paid to state and local governments.

President Reagan's tax plan seems to set the traditional relationship between government and the private voluntary sector on it's head. Mr. Reagan proposes to continue tax deductions for donations for private charitable purposes while eliminating tax deductions for publicly levied taxes that are the base of support for public services. Such a proposal makes little sense from a public policy point of view. State and local taxes are levied through democratic political procedures in order to support the core services of eduction, sanitation, health, transportation, nutrition and other public concerns. Charitable giving is usually a supplement through which private organizations provide additional support for many of these same services. No one would argue that private, non-profit charitable institutions are capable of performing the primary role in the provision of these vital services, yet, the proposed tax bill seeks to make contributions for private supplementary services deductible while eliminating the same deduction for public compulsory support of these same services. As I stated earlier, this change in policy makes no sense, and if enacted, will work to the detriment of public services and those citizens who depend on them.

The AFT does not oppose the allowances in the President's bill for charitable giving, just as we did not oppose allowing non-itemizers to claim a charitable deduction in the 1981 tax bill. We only wish to point out that if deductibility of state and local taxes is lost, a massive inequity will be created as support for private giving stays tax deductible while support for public giving through taxation becomes taxable.

President Reagan's tax bill does not really seek to end tax preferences in our tax code. The tax bill as proposed continues the process of picking winners and losers through tax preferences.

Federal support for all public education through deductibility amounts to approximately $16.5 billion according to a survey done by the AFT. If this federal support is lost, state and local taxpayers will be required to increase their tax liability by an amount greater than the budget for the U.S. Department of Education as proposed by the President for FY'86. As education loses tax support, loopholes for the oil industry and for the corporate sector go unchallenged. Ironically, private sector education will benefit from charitable giving, while public schools may have to endure a 20% decline in property tax support. This is the unexamined impact of the President's tax plan.

It is important to note that education reform and improvement is now a national issue. This has happened in part because of the efforts President Reagan made in 1983 to call attention to our nation's educational shortcomings. Some of us who had been attempting to focus the nation's attention on the need to improve education welcomed the President's leadership. The AFT invited President Reagan to present his view on education reform to our 1983 convention. The President made a compelling case for education reform as a national issue. Mr. Reagan, however, does not believe that the federal government should pay any of the costs for educational improvement.

By and large, states and localities have borne the burden of financing school improvements. Federal cutbacks have been enacted across the board for federal programs that aid state and local governments, yet support for education has increased. The taxpayers have been willing to shoulder the cost of increased education spending in return for improvements in education policies. We, in the AFT fear that if federal deductibility of state and local taxes is lost the efforts now underway to improve education will be stymied. Loss of deductibility could cause a serious erosion in educations' tax base.

Most of the testimony that this Committee will receive will be based upon projections of conditions that may result from one change or another in tax policy. For state and local governments we must rely upon the so called "tax price" method of calculating the effects that loss of deductibility would have on the ability of state and local government to finance education.

Since 1956, when Mr. Charles Tiebout published an article entitled, "A Pure Theory of Local Expenditures" in The Journal of Political Economy, "tax price" has been a key concept in public finance literature. The Tiebout model envisions taxpayers "voting with their feet" to find the package of services and taxes that suit their desires. This model has been challenged over the years but no one doubts that government services carry an identifiable price. High officials in the Treasury Department have been known to talk about voters/taxpayers "voting with their feet" to avoid paying high state and local taxes.

The method of calculating the true price of services goes relatively unchallenged: The national average marginal rate under current law is about 28%. Nationwide, under current law, the average itemizing taxpayer pays the following "tax price" for state and local services.

T.P. = $1 (1 marginal tax rate)
T.P. = $1 (1- .28)
T.P. = $0.72

The average itemizing taxpayer is paying $.72 for every dollar received in state and local services. Loss of federal deductibility would mean that itemizing taxpayers would be paying full price for the same services. The loss of deductibility would therefore cause a perception of a sharp increase in the tax price of services such as education. Other favorable developments such as lower rates would not offset the perception that state and local taxes would be sharply higher. The following result would occur:

Current law "tax price" State and Local Services	$.72
Treasury Tax Plan: New Tax Price for S&L Services:	$1.00
Perceived Increase "tax price"	.28
Percentage Increase in "tax price":	.28/.72 = 39%

Some generally accepted guidelines exist for calculating the effect of a 39% increase in the real property tax price. Although there are variations, the Congressional Research Service maintains that "price elasticity" for state and local services is about -0.5. This means that over time voters are likely to respond to a 39% increase in a tax price by demanding that it be cut in half.

If this expectation is accurate we can anticipate a 20% cut in local revenue for education. A revenue cut of that magnitude would certainly result in a similar spending cut.

Because education is still heavily financed by the property tax the "tax price" theory is easily applied. Other public services which depend on state income or sales taxes might not be so subject to "tax price" sensitivity and it is possible that base broadening in the Reagan plan could offset losses. We do know that increasing the tax price will result in a reduction of spending at all levels of government. The Advisory Committee on

Intergovernmental Relations states that local property taxes pay for about half of the state and local cost of elementary and secondary education. The federal government pays about 7%.

The President and Treasury Department have made elimination of deductibility for state and local taxes their number one priority. Presidential Assistant Patrick Buchannan has stated that the elimination of deductibility is aimed at the "neo-socialist" states of the Northeast. The President's plan however, is loaded with tax references for politically powerful elements in the private sector. President Reagan would have us believe that "reform" now depends on more sacrifices from the public sector. This is Mr. Reagan's preference, not a true statement of fact. This current opportunity for tax simplification should not become a contest between public and private needs. It is necessary, however, to point out that the President's philosophy seems to be that economic growth and prosperity must come at the expense of the public sector. The AFT believes that quality education, good mass transit, health care and transportation are indispensable to national economic growth and prosperity. Loss of deductibility will impact negatively on all elements of the public sector. It has become clear over the last few years that the availability of public services, especially education, is an important consideration in decisions made by business leaders. A healthy public sector is just as important as a healthy private sector in the equations of economic growth. The Reagan Administration has stated that rate reduction is impossible without the $38 billion in revenue taken from the public sector through the elimination of deductibility for state and local taxes. We believe that it is very possible to have a tax reform bill and maintain deductions for state and local taxes.

AFL-CIO President Lane Kirkland has presented testimony to this Committee that outlines where revenues can be found to fund tax rate reductions. The AFT endorses the AFL-CIO proposals as the best way to not only reduce tax rates, but restore a measure of equity to the federal tax code.

Like the AFL-CIO, the AFT believes that other elements of the Reagan tax plan must be revised by the Congress. The proposed new taxes on life support benefits such as health insurance, workers compensation, black lung and death benefits are totally wrong and should be rejected by the Committee. The AFT also opposes the Administration's plan to further tax unemployment compensation.

The Administration proposals in the retirement plan area are of serious concern to the AFT and its members. Many of these highly technical proposals would severely discourage teachers from participating in retirement programs, and would greatly reduce the opportunities for them to accumulate necessary levels of retirement income. For example, we are concerned that the proposed changes in the taxation of contributory pension plans will have a particularly harsh impact on teachers and other public employees who commonly participate in these plans. We also are concerned that the proposed restrictions on the payment of benefits under tax-deferred annuity programs (sec. 403(b)), and the proposed 20 percent penalty tax on so-called "pre-

State and local tax deductions are not a special interest, rather they are a key to improving education and many other public sector contributions to our nation's economic growth. Retaining federal deductibility preserves the principle that we should not be required to pay taxes on taxes legally levied by other levels of government.

STATEMENT BY WILLIAM LUCY, SECRETARY-TREASURER, AMERICAN FEDERATION OF STATE, COUNTY AND MUNICIPAL EMPLOYEES, WASHINGTON, DC

Mr. LUCY. Thank you very much, Mr. Chairman.

With me this morning is Iris Lav from our Department of Public Policy.

Mr. Chairman, on this subject of tax reform, as we talked to working people around the country, whether low income or middle class Americans, we have heard a clear indication that they want tax reform. Working men and women know that they are carrying an unfair share of the total burden; however, that does not mean that any revision that is called "reform" will do. The tax reform they desire must be based on three principles:

First, it must be fair. Every corporation and every individual must pay a fair share.

Second, it must raise enough revenue to make the Federal Government pay for itself.

And third, it must enhance and not destroy the integrity of our Federal System of Government.

The President's proposal does not measure up on any of these standards. The corporate tax reform, in our opinion, is a sham. It ignores the Treasury Departments's excellent economic depreciation scheme and instead proposes depreciation that is even more generous than the excesses of the current system.

On the individual side, the end result is elimination of progressive taxes. The capital gains tax rate would be reduced by over a third, and the maximum tax rate cut in half since 1980.

New regressive features would be added: A health insurance tax that takes five times the percentage of income from a near-poverty-level family than it does from a person earning $100,000, the child care deduction instead of a credit, and taxation of unemployment and workers compensation.

The real losers under this plan are the vast majority of Americans, including the broad middle class. The will lose from the elimination of the deductibility of State and local taxes. Along with the poor, eliminating the deductibility in the long run will seriously injure the middle class—working people who have just managed to buy a home, who need quality public schools for their children, who are concerned about the safety and cleanliness of their neighborhoods, and who use public recreational facilities. The middle class will lose as their property taxes go up and the value of their homes become at risk. They will lose the public services upon which they depend. It is the broad middle class, not a small minority of taxpayers, who use the deduction. Of the 33 million returns with the deduction, 27 million had incomes between $10,000 and $50,000 per year. This "small minority" paid 72 percent of all Federal income taxes paid.

The middle class is the backbone of the taxpaying American public, and they would be hurt by the elimination of deductibility. Median income families in many States, particularly if they have two earners, will see their Federal taxes increase. The middle class also pays the bulk of State and local taxes, and they will lose as these taxes everywhere become more regressive. Absent deductibility, the incentive and consistency for progressive taxes will disappear.

This tax package will also destroy the central cities of this Nation, not just in the Rust Belt but everywhere. Taxes are one-third higher in central cities than in their surrounding suburbs, nationwide. These higher taxes reflect the higher cost of cering for the poor, the elderly, and the disadvantaged. Ending deductibility would encourage further the middle class flight to the suburbs. Central cities will be left with the same level of needs and a far smaller tax base from which to meet those needs.

State and local governments are the frontline problem-solvers on this country. They must have the resources to carry out that job. elimination of deductibility will force immediate service cuts, will limit the ability to provide service and meet needs in the future, will make State and local government taxes more regressive, and will set off an incredibly divisive urban-suburban competition. This, Mr. Chairman, is not federalism; this is destruction.

I am very disturbed by the growing number of reports showing that this plan will lost tens of billions of dollars because of a failure to make corporations pay a fair share and because of the generosity of this plan to the wealthier citizens of this country.

The question is: Whose taxes, in the end, will be raised to make up the difference? If corporations and the wealthy are sacred and the poor cannot pay more, it would be our members, middle class workers, who would bear the brunt.

In summation, I do not think that this plan can be called "reform" in any sense of the word; it is a step backwards. I think this committee should reject the administration's proposal. However, it most certainly should move forward on tax reform.

I hope you will take a clean look at tax reform, starting from the basic principles of revenue adequacy, fairness, and federalism. And certainly, Mr. Chairman, if you do this you will have the support of our institution as well as many others across this country who are concerned with the question of tax reform.

Mr. CHAIRMAN. Thank you, sir.

Mr. Schaitberger.

[Mr. Lucy's written testimony follows:]

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STATEMENT OF

WILLIAM LUCY
INTERNATIONAL SECRETARY-TREASURER

AMERICAN FEDERATION OF STATE,
COUNTY AND MUNICIPAL EMPLOYEES

ON

THE PRESIDENT'S TAX REFORM PROPOSAL

BEFORE THE

COMMITTEE ON FINANCE

U.S. SENATE

JULY 24, 1985

in the public service

SUMMARY OF PRINCIPAL POINTS OF TESTIMONY

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I. The President's proposal is not fair tax reform. It will increase, in many cases, the overall burden borne by low and middle-income wage earners and worsen the plight of the poorest citizens of this country. 2

A. The President's plan ignores the Treasury Department's original indexed economic depreciation scheme and instead substitutes a complex, back-loaded system that is even a bigger give-away than the current ACRS. 2

B. The President's proposal to include in a worker's gross income the first $10 per month for single coverage or $25 per month for family coverage of employer-paid health insurance is an extremely regressive proposal 5

C. Transforming the child care credit to a deduction is a direct income transfer from lower income to higher income taxpayers 5

II. Elimination of the federal deductibility of state and local government taxes will have an extremely adverse impact on low and middle-income citizens 6

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D. Any alleged base-broadening resulting from the President's proposal will not compensate state and local governments for the loss of deductibility 11

III. There are alternatives which would provide meaningful tax reform for low and middle-income citizens 13

Mr. Chairman, I am William Lucy, International Secretary-Treasurer of the American Federation of State, County and Municipal Employees. I also serve in the capacity of President of the Coalition of Black Trade Unionists. AFSCME represents 1.4 million public employees throughout the country, located in 48 states.

AFSCME has long advocated reform of our tax system, and surely that loophole-ridden system cries out for reform.

We believe that genuine reform must follow certain basic principles. The federal tax system must be one that raises adequate revenues. It must raise those revenues based on the principles of progressivity, fairness and federalism. Progressivity means that the rich, as well as working Americans, contribute based on ability-to-pay. Fairness means that profitable corporations pay their fair share for the services that make their businesses possible. And federalism means that state and local governments' ability to also raise adequate revenues in a fair and progressive manner must not be impaired.

I spend much of my time traveling the country, from one end to the other, talking to working people. Americans want tax reform. They want tax reform because ordinary working men and women know that they are carrying an unfair share of the total burden. We printed the poster "I Pay More Federal Income Taxes Than General Electric, General Dynamics, Dow Chemical, W.R. Grace & Co., Lockheed, and Boeing, All Put Together" in the newspaper those posters have gone up on walls across the country. The current tax system is unfair, and people know that it is unfair.

Unfortunately, the President has not proposed the type of tax reform for which people are crying out, but rather exploited this opportunity to extend his ideological views. The tax reform that the President has proposed is nothing more than an extension of his policy of tax and budget cuts for federal, state and local governments.

Fairness

On the corporate side, the reform is a sham. It ignored the Treasury Department's excellent indexed economic depreciation scheme, and instead proposed a complex, back-loaded system that is even a bigger give-away than the current ACRS. According to the Administration's own numbers, in 1990 the Treasury Department's scheme would have increased revenues by $68 billion; the President's raises only $15 billion. According to the Congressional Budget Office, the Administration's CCRS is more generous -- loses more revenue, in each of the next 15 years except 1989 and 1990. We have not one shred of evidence that the exorbitantly expensive 1981 depreciation change in any way increased investment or improved the economy. The weight of evidence is in fact on the other side. There is much justification for returning to a depreciation system based on economic life. We see no justification at all for creating an even larger, revenue draining, depreciation loophole.

I regard the substantial amounts of revenue lost through the CCRS proposal -- an admitted $53 billion difference between the Treasury and the President's plan in 1990 -- as money taken directly out of the pockets of our members and out of the budgets of state and local governments. It is a major cause of the inadequate revenues this plan raises, and thus will be used, as was the 1981 tax act, as an excuse to further cut the services that are the lifeline for the poorest people of this country.

It is interesting to note that the President's plan even acknowledges the Treasury's depreciation system as the true depreciation system, the fair one. It says that foreign property would be recovered under a system of "real economic depreciation", referring to that in Treasury I. It also uses Treasury I's depreciation system as its standard of comparison for the minimum tax. That is a clear admission, in the President's own plan, that its CCRS differs greatly from an appropriate depreciation system.

I am very hard put to believe the President when he says that all corporations will be put back on the tax rolls. With as many loopholes as this plan leaves intact, and with a fake minimum tax that does not collect as much as $1 billion in any year, a minimum tax which is that in name only, it simply cannot be true.

The reduction in the capital gains rate is still another extension of the 1981 damage. The maximum rate was reduced in

1981 from 28% to 20%, and the plan would push it down again to 17.5%. Again, there is no economic rationale for doing this. Turning ordinary income into capital gains is the basis for an entire tax shelter industry, and this provision will help that industry continue to thrive.

Finally, cutting the maximum tax rate in half, from 70% to 35% since 1980, is an outrage to every hard working, wage earning person in this country. Our members were outraged by the huge giveaways to wealthy individuals in the 1981 tax bill from which, I might mention, they were largely excluded. The damage to progressivity done in 1981 will be compounded by a further cut in the tax paid by upper-income individuals.

If these rate cuts and tax shelter encouragements are enacted, I think we will have to revise the poster that I mentioned and list, along with the companies that pay no tax, the millionaire executives of these or other major corporations in this country.

I think the President realized that these features of his tax proposal that I have just mentioned would be totally unpalatable to most Americans. So he put in a Sweetener. That sweetener is low-income tax relief. On its face, the plan gives substantial relief to low-income wage earners. But that is on its face. In the total picture, this crumb thrown by the tax proposal has its hidden costs.

First, it does not even bring low-income wage earners back to their tax position in 1979 before he took office. The federal tax burden on poverty-level workers -- their income and Social Security taxes as a percentage of income -- would still be higher in 1986 under this plan than it was in 1979. For a single-parent family of four at the poverty level, this proposal would leave the tax burden three times as high as it was in 1979 -- 5.6% of income under this plan in 1986 versus 1.8% of income in 1979. By way of comparison, a family of four with an income of $100,000 in 1979, whose income grew at the same rate as that of the poverty-level family, would see its taxes cut by one-fifth.

Second, a regressive tax on employer-paid health insurance would be added to the code, a tax that takes five times the percentage of income from a family at 125% of the poverty level than it does from a person earning $100,000. AFSCME strongly opposes any and all proposals to tax basic workplace benefits.

Third, the plan would wipe out the child care credit, a credit which makes it possible for many to work. It would hurt single parents and families in which two wages are needed for a decent level of living. It would replace that credit with a deduction. The deduction would increase from 20% to 35% the level of child care subsidy for upper-income taxpayers who can itemize, while the subsidy for the low income family would drop from 30% to zero.

Fourth, the plan would penalize ordinary working folk at the time when they can least afford to bear an additional tax burden. The taxation of unemployment compensation, and workers' compensation, and black lung compensation shows an insensitivity beyond words.

Federal Revenues

Finally, I do not think we can ignore the fact that this plan would actually reduce revenues of the federal government. I know there is some controversy over how much they would be reduced, but I am very concerned about the reports from the Congressional Budget Office, Wharton Econometrics, Senator Moynihan and others that suggest additional deficits in the tens of billions of dollars. That is a true hidden cost of this tax plan. It may be giving some low-income federal tax relief, but the inadequate revenues will be used, as they have been used time and time again in this Administration, as an excuse to cut back on the vital services on which these same low-income workers, and those even less fortunate, depend.

Federalism

The inadequate revenue does not stop at the federal government level. The elimination of the deductibility of state and local taxes in this proposal would export that inadequacy. It is nothing short of a reversal of more than 120 years of federalism.

Thanks to the efforts of Congress and many of the members of this Committee, the President is no longer able to cut AFDC and Medicaid at the federal level. So he's found a new tack. This tax proposal would force the states to make the cuts themselves.

Eliminating deductibility will put a severe fiscal strain on states. It is an unfair "double whammy" on state and local governments, coming at a time when cuts in grants-in-aid are seriously hurting the ability of state and local governments to maintain services from their own revenue sources. It will first hurt states that have a higher level of taxation and spending because they have 1) a higher level of need due to their population characteristics, and 2) have chosen to meet that need at a responsible level.

If we take just one example, AFDC, we can get a clear idea of who will be hurt. There are 17 states (including the District of Columbia) that are identified by the Advisory Commission on Intergovernmental Relations as losing from the elimination of deductibility. 11 of these 17 states provide maximum AFDC grants that are at least 90% of their own established standard of need. In contrast, 17 of the 34 states that are considered winners from the elimination of deductibility -- at least initially -- pay AFDC recipients only 75% or less of their standard of need. How long will a New York, a California, a Delaware, a Hawaii, a Minnesota, a New Jersey, an Oregon or a Rhode Island be able to provide 100% of the standard of need, if deductibility is eliminated? The answer is, not very. These states will be penalized for accepting and fulfilling a responsibility that should be routine in this nation of ours. What has not been able to be accomplished at the federal level, the elimination of deductibility will force states to do.

The President's agenda of making taxes less progressive will also be forced onto the states. States that have the most progressive tax systems will bear the brunt of the harm from elimination of deductibility. Seven of the 10 states that have been identified as having the most progressive tax systems are among the 17 states that are net losers from the elimination of deductibility. Nine of the 10 states that lose the least from the elimination of deductibility are also included among the 10 states with the most regressive tax systems. Eliminating deductibility will create immediate pressure to reduce the progressivity of state and local tax systems. Upper-income taxpayers will not accept the greater share of the burden if it cannot be offset against federal taxes. States that now have progressive systems will be pushed to make them more regressive. And states that now have relatively regressive systems and that are considering instituting more broad-based progressive taxes (such as Tennessee, Texas, Connecticut and Washington) will have little chance of doing so absent federal deductibility.

The budget actions taken and proposed during this Administration have eliminated many forms of aid to urban areas, ranging from education for the disadvantaged, to job training, to social services, to subsidized housing, to urban development action grants, to general revenue sharing. Again, this tax package furthers those goals and attempts to accomplish much of what the Administration has not been able to do through the budgetary process.

Central cities will be particularly hard hit by this proposal. The U.S. Advisory Commission on Intergovernmental Relations has shown that taxes in 1981 were an average of 37% higher in central cities than in their surrounding suburbs. This pattern holds nationwide. It is as true in Atlanta and in San Antonio as it is in Baltimore and Portland, Oregon. These higher taxes reflect the higher costs of caring for the poor, the elderly and the disadvantaged.

Ending deductibility will encourage further middle class flight to the suburbs at a time when this has finally stabilized or even reversed in some places. Fewer middle class people will choose to stay in cities paying higher taxes if they no longer receive a partial federal tax savings from doing so. Central cities will be left with the same level of need -- it will only be those who can afford it who will vote with their feet -- and a far smaller tax base from which to meet those needs.

State and local governments will be facing many new and increased needs in the near future. We have a growing elderly population, we have increasingly crowded prisons, we have a new baby boomlet, and we have a crumbling infrastructure. The President's proposal is destroying the basic foundation of federalism in this country that allows state and local governments to meet these needs. The President says he believes in federalism and he believes in state and local control, but even one of Mr. Reagan's philosophical compatriots, former Congressman Barber Conable, says that this tax plan "strikes a terrible blow at federalism".

State and local governments are the critical deliverers of service in this country. It has always been that way. They are the front line problem solvers, but they must have resources.

The elimination of deductibility will force immediate service cuts, will limit the ability to provide services and meet needs in the future, will make state and local taxes more regressive, and will set off an incredibly divisive round of urban/suburban competition. That is not federalism. That is destruction.

Before leaving the subject of deductibility, I would like to take on two arguments that are often made by opponents of deductibility: One is the cross-subsidy argument that low-tax states are now subsidizing high-tax states. The other is the base-broadening argument, which says that this plan will provide additional resources to state governments, through its base-broadening features, to offset the loss in deductibility. Both have more elements of myth than reality.

First, the cross-subsidy argument. This is one country. Some degree of cross-subsidy in tax systems and in federal spending is inevitable. But of all the types of subsidies that exist, the opponents of deductibility are looking at only one kind, the deductibility of individual state and local taxes. When President Reagan spoke in Oklahoma last month, he said that he didn't think the folks in Oklahoma, and Texas and Montana should have to subsidize states that "have not yet learned to say

'No' to special interest groups and higher taxes". Well, I'd ask you to note that Oklahoma, Texas, Montana, Wyoming, Alaska and Louisiana are all energy producing states that derive a substantial proportion of their revenue from severance taxes. These taxes will remain deductible as business taxes, yet every time a person in a northeastern state buys a gallon of gasoline or heating oil, every time a midwestern industry uses a ton of coal, they are subsidizing, in the price of that gas or oil or coal, the services provided by the residents of these severance tax states. I don't hear anybody complaining about this cross-subsidy.

Indeed, if the objection to deductibility is that it forces taxpayers in low-tax states to subsidize "overly generous" services received by residents of high-tax states, then Alaska and Wyoming might have to be considered the worst offenders -- they rank No. 1 and No. 2 in per capita state and local government spending. New York, the next highest spending state, is fully 22% below Wyoming in per capita expenditures. This issue is certainly a red herring .

Finally, I'd like to speak briefly to the base-broadening issue. Base-broadening will not compensate state and local governments for the loss of deductibility. Base-broadening will be minimal at the state level, and almost nonexistent for local governments. Only a very few local governments have the authority to levy personal or corporate income taxes. Of the some 54,000 local jurisdictions in the United States, less than three-tenths of one percent have local income taxes whose base might be broadened. Property taxes provide 76% of local tax revenues, and local governments will get no compensation from the increase of the real cost of these property taxes on their residents. Indeed, most local governments will have declining tax bases if the President's plan is implemented. Most economists believe that the value of real property will decline as the result of the new limits on a number of its tax advantages. As assessments decline, local governments will have to either raise their property tax rates -- never a politically popular thing to do -- or face declining revenues.

Even at the state level, base broadening is far less than an established fact.

The single largest base broadener in the President's plan is the elimination of deductibility. No state allows an income tax deduction for state income taxes paid, so immediately 57% of that evaporates. It is unreasonable to assume that states will disallow the deduction of their own sales taxes. They are likely to consider that an unfair tax on a tax. Finally, the state deductibility of local property taxes is widely viewed, and even budgeted, as a form of state aid to local governments. And the property and income taxes are often coupled to provide circuit breaker tax credits for property taxes paid.

Nor will the repeal of the investment tax credit, another big ticket item in the plan, have much effect on states. Only three states -- Colorado, Idaho and Vermont -- allow a portion of the federal investment tax credit on their income tax returns, and only they will be affected.

The depreciation allowance could be a possibility for base broadening, but in fact is a base narrower in the President's plan. If, as the CBO calculates, CCRS will result in a revenue loss compared to ACRS at the federal level in 13 of the next 15 years, then it will also cause proportional revenue losses in each of the states with tax systems coupled to federal depreciation methods.

There are a number of other base-narrowing features of the President's plan. The largest of these, outside of depreciation, are the expansion of Individual Retirement Accounts and the 10% deduction for corporate dividends. If states are coupled to federal tax definitions, they will lose revenue from these provisions, as well. Indeed, it is likely that most states will lose revenue overall if the plan were enacted. I think the burden of proof rests on those who assert base-broadening from this tax plan. Thus far they have failed to produce that proof.

In summation, I do not think that this plan can be called "reform" in any sense of the word. It is a step backward.

I think this Committee should reject the Reagan proposal, but it most certainly should not reject the concept of tax reform. Instead, it should take a clean look at tax reform, a fresh look, starting from a set of principles of fairness and equity. These principles must include: 1) Adequate revenues, so that citizens will not lose government services as much or more than they have gained from tax cuts. 2) A redress of the depreciation cuts made in 1981 that virtually eliminated the corporate tax and indeed created a negative corporate tax in many instances. 3) An improvement in the progressivity of the total federal tax system, considering both income and Social Security taxes, working toward an improvement that would benefit the middle class, as well as the working poor. It may be faddish to consider progressivity a dirty word, but it has worked for nearly 75 years in this country, and it has worked well. 4) Truly eliminating taxes on people below the poverty level. It is a scandal to tax away income below a minimum subsistence level. And finally, any change must 5) enhance the ability of state and local governments to develop and maintain an adequate revenue base and to work toward more progressive tax systems at that level. Giving with one hand and taking away with another may seem like popular politics now, but I don't think it will be too long before the people of this country realize what has happened to them.

I know that I have outlined a tough job here. But if the Committee strikes out on a road to real tax reform, based on the principles of revenue adequacy, fairness, progressivity and federalism, I can assure you that you will have the support of AFSCME and all Americans.

Table 1

Federal Tax Burden on a Single Parent Family of Four with Poverty Level Wages 1979 and 1986 President's Proposal

	1979 w/o child care credit	1979 with child care credit	1986
Poverty Level Income, Family of Four	$7,412	$7,412	$11,457
Employer-paid Health Insurance			300
Gross Income	$7,412	$7,412	$11,757
Less: Personal Exemptions	4,000	4,000	8,000
Standard Deduction	2,300	2,300	3,600
Taxable Income	$1,112	$1,112	157
Income Tax Liability Before Credits	156	156	24
Less: Child Care Credit		200	
Less: EITC	322	322	227
Income Tax	-166	-322	-203
Social Security Tax	454	454	841
Total Federal Tax	288	132	638
Federal Tax as Percent of Income	3.9%	1.8%	5.6%

Source: 1979 data from Children's Defense Fund, The Impact of Federal Taxes on Poor Families. 1986 data calculated by AFSCME.

Table 2

Federal Tax Burden on an Upper Income Family of Four 1979 and 1986 President's Proposal

1979			1986		
Gross Income			Gross Income		
			Employer-paid Ins.	$ 600	
Earner #1 Salary	$50,000		Earner #1 Salary	77,287	
Earner #2 Salary	25,000		Earner #2 Salary	38,644	
Interest	10,000		Interest	15,457	
Dividends	7,500		Dividends	11,593	
Long-term Capital Gains	7,500		Long-term Capital Gains	11,593	
		$100,000			$155,174
Less Exclusions			Less Exclusions		
Dividends	$ 200		50% of LTCG	($ 5,797)	
60% of LTCG	4,500	($ 4,700)	Maximum IRA	(4,000)	($ 9,797)
Equals: Adjusted Gross Income		$ 95,300	Equals: Adjusted Gross Income		$145,377
Itemized Deductions			Itemized Deductions		
@24.18% of AGI	$23,044		@16.65% of AGI	$24,205	
			For dependent care costs	4,800	
Less ZBA	(3,400)		Less ZBA	(4,000)	
Equals: Excess Itemized Deductions		($ 19,644)	Equals: Excess Itemized Deductions		($ 25,005)
Less: Personal Exemptions (4)		($ 4,000)	Less: Personal Exemptions		($ 8,000)
Equals: Taxable Income		$ 71,656	Equals: Taxable Income		$112,372
Tax Liability on $71,656:		$ 25,973	Tax Liability on $112,372:		$ 28,830
Less: Maximum Dep.Credit:		(800)	Plus: Social Security Tax:		5,766
Equals: Federal Income Tax Liability		$ 25,173	Equals: Total Federal Taxes		$ 34,596
Plus: Social Security Tax		2,808			
Equals: Total Federal Taxes		$ 27,981	As % of income		22.3%
As % of income		28.0%			

Table 3

States That Would Lose[1] From Elimination of Deductibility: AFDC Spending and Tax Progressivity

	AFDC % of Need[2]	Index of Progressivity[3]
California	100%	195
D. C.	51%	138
Delaware	100%	191
Georgia	55%	112
Hawaii	100%	157
Massachusetts	95%	85
Maryland	79%	94
Michigan	91%	99
Minnesota	100%	221
New Jersey	100%	66
New York	100%	155
Oregon	100%	125
Rhode Island	100%	97
South Carolina	76%	152
Utah	54%	90
Virginia	90%	106
Wisconsin	85%	101

	Average	Average
Winning States	75.6%	93.6
Losing States	86.8%	128.5

1/ States that have been identified by the Advisory Commission on Intergovernmental Relations (ACIR) as initially losing from the elimination of deductibility. This is not to say that other states would not lose in the future. Source: Daphne A. Kenyon, Federal Income Tax Deductibility of State and Local Taxes (Discussion Draft prepared for the U.S. Department of the Treasury study on Federal-State-Local Fiscal Relations), April 1985, Table 6, page 16a.

2/ AFDC maximum payments as a percent of the minimum standard of need established by that state. Source: Committee on Ways and Means, U.S. House of Representatives, Background Material and Data on Major Programs Within the Jurisdiction of the Committee on Ways and Means, February, 1984, Tables 7 and 8.

3/ The progressivity indexes were computed as follows for selected state and local taxes in the largest city in each state: taxes as a percentage of income at the $100,000 level divided by taxes as a percentage of income at the $17,500 level (multiplied by 100). Indexes greater than 100 indicate a progressive tax structure; indexes less than 100 indicate a regressive tax structure. Taxes included are state and local individual income and general sales taxes and the local tax on real property. Source: Advisory Commission on Intergovernmental Relations, Tax Burdens for Families Residing in the Largest City in Each State, 1982, Staff Working Paper #3, April 1984, Table A-5.

Table 4

Examples of 1982 State Tax Burden on $17,500 Income Family of Four

	State Individual Income Tax	State General Sales Tax	Total State Tax
Gainers from Elimination of Deductibility			
Mississippi	16	325	341
Alabama	268	226	494
Arkansas	184	186	370
West Virginia	252	202	454
Losers from Elimination of Deductibility			
New York	256	183	439
California	116	208	324
Michigan	-135	184	49
Delaware	321	0	321

Source: Advisory Commission on Intergovernmental Relations, "Tax Burdens for Families Residing in the Largest City in Each State, 1982." State Working Paper #3, April 1984.

STATEMENT BY HAROLD A. SCHAITBERGER, DIRECTOR, DEPARTMENT OF GOVERNMENTAL AFFAIRS AND PUBLIC RELATIONS, INTERNATIONAL ASSOCIATION OF FIRE FIGHTERS, AFL-CIO, WASHINGTON, DC

Mr. SCHAITBERGER. Thank you, Mr. Chairman.

The International Association of Fire Fighters, which represents 170,000 professional firefighters across the United States, would like to thank you and the committee for the opportunity to present some views concerning the tax reform proposals before your committee.

In reviewing the current tax proposals under consideration it is important for me to state that the IAFF believes all American workers support a fair tax structure. It is unfortunate, however, that too many of those workers are convinced that tax legislation is crafted by special interests that desire to avoid and evade their fair share of tax liability.

We believe your committee, Mr. Chairman, has the opportunity now to develop a less complex, understandable, and equitable Tax Code. While we laud your efforts, we nevertheless have several reservations that many aspects of the President's most recent tax proposals will result in less than fairness, growth, and simplicity—despite the statement from the President during his May address to the Nation that, and I quote, "A second revolution has arrived that ensures tax equity for all."

We have addressed in our statement several provisions in that proposal which would severely restrict the ability for State and local governments to maintain essential services, and other proposals, which you may not have heard much about, which would seriously reduce the retirement benefits earned by millions of American workers.

One of the most harmful provisions, as we discuss on page 2 of our testimony, is the 20-percent excise tax on any nondisability retirement benefit received by any worker prior to the age of 59½. Although this tax can be reduced to 10 percent if the individual uses the retirement distribution for the purpose of purchasing a primary residence, for the college education of a dependent, or even to replace unemployment benefits during a period of unemployment, it is simply an unfair tactic alleged to close loopholes but in reality forcing individuals to retire later.

To the average firefighter who would retire on a modest $15,000 annual retirement annuity after 30 years of service, this would mean a $3,000 tax off the top which, in itself, would not be deductible. In addition, that employee would still be liable for the Federal and State income tax for the entire $15,000 annuity. Couple this with another provision in the tax reform proposal which would require an individual to pay income tax from the first day that the retirement benefits are received, and you have a wholly unfair situation. For professional firefighters and law enforcement officers in particular, this provision would be devastating.

Another provisions in the President's plan would tax workmens compensation and disability benefits. Again, we believe this to be unfair and an inequitable proposal. Currently, job-related disability benefits are paid to individuals, basically replacing their current take-home income at the time of disablement. These benefits are usually approximately two-thirds of their gross income at the time of disability. Now the Government wants tax those disability benefits placing these individuals at lower income levels than they received while working. It only seems fair that if a worker is disabled in the course of performing his duties, he and his family should not be penalized for maintaining their standard of living through tax structure.

Several of the current retirement-related proposals, which we have identified in our testimony, would severely harm all middle-income workers who rely on their retirement plans for postwork income and not tax-sheltering schemes.

While considering these proposal and developing a final bill for passage, we ask the committee not only to look for ways of eliminating abuse and misuse but to help ensure that working individuals can rely on their retirement programs to be an integral component of their postemployment compensation.

I would also like to briefly mention and extend to the chairman our appreciation from the professional firefighters of this Nation for his ardent support and continued opposition to the taxing of employer-paid benefits. We certainly associate our views with those of the previous witnesses this morning and hope that the chairman will continue in those efforts.

I would also like to briefly mention the elimination of the deductibility for State and local taxes, as others have mentioned. As we point out in our statement, we believe it will have catastrophic effects on the ability for State and local governments to maintain and provide essential services for the public.

It is startling that, after President Reagan instituted his New Federalism in 1981, shifting the burden of providing vital services to State and local governments, he would now cut the ability of the support system that provides the resources need to maintain and enhance these services.

We are here today not only to point out our special interests, which we hope this committee will modify, take into consideration, and possibly embrace but to make several suggestions for creating a fair and adequate tax system. Our international points out several specific recommendations, which can be found on pages 10 and 11 of our statement.

In conclusion, Mr. Chairman, it is not the position nor the responsibility of the International Association of Fire Fighters to understand the tax implications for all industries and sectors in our economy. We do, however, have the responsibility for protecting and enhancing the retirement income security of our members and maintaining an effective and efficient fire protection service for this Nation. We stand ready to assist you in your efforts, and we would be glad to answer any questions the committee may have at that time.

Thank you.

The CHAIRMAN. Thank you.

Mr. Biller.

[Mr. Schaitberger's written testimony follows:]

TESTIMONY
BEFORE THE
SENATE FINANCE COMMITTEE
ON
PRESIDENT REAGAN'S PROPOSAL FOR COMPREHENSIVE TAX REFORM

July 24, 1985

HAROLD A. SCHAITBERGER
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Mr. Chairman, members of this distinguished committee, my name is Harold A. Schaitberger, Director of Governmental Affairs for the International Association of Fire Fighters, AFL-CIO-CLC, representing more than 170,000 professional fire fighters throughout the country. I would like to thank you for the opportunity to discuss our President's tax proposals and specifically how the changes will affect fire fighters and other public employees.

We commend you for your positive efforts in struggling to formulate a more fair and equitable tax proposal. Rate reductions, increasing the personal exemption, and increasing the zero bracket amount for the poor, are all long overdue changes. We also are enthusiastic that our conservative friends in public office have finally succumbed to the realization that despite torrents of dogmatic rhetoric the 1981 tax plan fulfilled everyone's worst prophesies and resulted in unprecedented massive deficits: it is clear that there is an urgent need for fair and equitable reform as soon as possible.

While we laud your efforts we nevertheless have some reservations that some aspects of the President's tax proposals will result in less than "Fairness, Growth, and Simplicity". Despite the repetitious statements from the President that a "second revolution" has arrived that ensures tax equity for all, complete industries have been granted tax preferences unjustifiably which has stalled the revolution for the time being. Of course, there have been rationales why certain industries have received tax preferences and excuses why wholesale cut backs on the less advantaged have been herded through the Treasury's tax mill.

One point that we must respectfully express our vehement opposition to is the President's tax proposal to penalize early retirement distribution from tax-favored retirement plans because of the adverse consequences it would have for the fire fighting and law enforcement officers in America.

Fire fighters and law enforcement officers are engaged in the dangerous professions of protecting our loved ones and property. Most fire and police personnel have the option of retiring after twenty or twenty five years of service sometimes prior to attaining age 50. Of course, the money they receive in the form of a pension is presently taxed as income.

If the President's plan is passed in its present form, the pension that some fire fighters and police officers receive will not only be taxed as income: it will be subjected to an additional excise tax of 20%! This is money that has been hard earned. This is money that must go towards paying bills and the necessities of life. This money is not any sort of bonus or lottery prize.

Let me illustrate how this will affect a fire fighter. Mortality studies reveal that an average fire fighter lives approximately ten years less than the average American--- Fire fighters contract cancer at two times the rate of the general population. Simply, because of the risks associated with the job of protecting everyone's children and property, fire fighters do not have nearly as many years to enjoy their pension benefits as most Americans who retire after long careers. We do not believe that the President or the Treasury Department deliberately decided to make such a callous proposal. We believe, shouldered with their enormous responsibilities, they overlooked how their proposal would affect the fire and police professions. We hope that due consideration will be given to these two important public employee groups and a change will be accordingly made.

Presently we have a rare opportunity to strangle the entrenched loopholes that major corporations have for so long unfairly prospered from. It is reprehensible that some of the largest corporations in our land have been able to skirt their tax responsibilities for so many years and pay either no tax or unbelievable as it may sound, receive refunds from the government. We all are aware of the horror stories such as W.R. Grace Co., the famed waste reformer, paying no federal tax. The 'Citizens for Tax Justice' has compiled an informative list that professionally exposes such corporate abuses. This extensive list should alarm all of us.

The most damaging aspect of allowing large coporations to avoid their responsibilities through technical accounting manuevers is that it erodes the average worker's confidence in his government. If a working person sees himself or herself paying more tax than a major corporation the government's credibility is seriously undermined. Once it is ingrained in a person's psyche that the government exists to secure and maintain the benefits of the corporations while ignoring the average citizen's interests, we all lose.

Considering that approximately thirty years ago corporate revenues contributed far more than 25% of federal revenues and today they comprise about 6 %, it is easy to conclude that there is a need to revamp the corporate tax structure.

The repeal of the deductibility of state and local taxes is a major source of revenue in the President's plan. This proposal is based on the short sighted theory that the repeal is warranted because the deduction for state and local taxes benefits a small minority of U.S. taxpayers at the expense of the great majority of Americans. Like it or not, the tax system encourages and conversely discourages particular policies for society to pursue. The tax system has been an important vehicle for achieving vital social and economic objectives.

The repeal of the state and local taxes is going to indisputably lead to a diminution of vital services for a great percentage of Americans. Public education, municipal sanitation services, and of course, fire protection and police services are going to be eventually reduced in many of our major states. Clearly strong pressure will be brought to bear upon state representatives to cut taxes if the deductibility is repealed. If there is less revenue to service the community, fire protection and police security will be among the essential services that will be reduced.

In human terms, rather than merely tax jargon, the loss of such vital services is potentially catastrophic. I do not have to tell anyone on the committee about the absolute neccessity of providing first class fire and police services.

Also, no one here needs to be reminded that without a quality education millions of our fellow citizens will not be able to propel themselves out of the quagmire of poverty that sadly engulfs and destroys the productive capacity of large sectors of our nation. The policy implications of repealing the state and local taxes has got to be weighed cautiously prior to anyone endorsing the proposal.

It is startling that after President Reagan instituted his "new federalism", that shifted the onus of providing vital services to states and local government, he would cut the feet out of the support system that would provide so many needed services. The President first shifted responsibility and now wants to eradicate the resources.

Furthermore, it seems that there is a prevailing sentiment that repealing the state and local tax deductibility will be only affect the well-to-do, since it is the wealthy that tend to itemize their tax forms. A sheer numerical analysis may even support this assertion. However a more comprehensive and far ranging analysis reveals that all of us are losers by repealing the deductibility. As I mentioned, if educational services are reduced the loser will not only be the student. The employer in need of skilled workers will also lose. As we move further into the high technology revolution, ample education for all Americans becomes an unqualified necessity. In the areas of our expertise---fire fighting---a wealthy person loses as much as a poor person if he or she falls victim to a devastating fire. God forbid that fires strike anymore Americans---but repealing the deductibility of state and local taxes will result in diminished fire and police protection.

* Section 3.06 of the proposal would eliminate the current tax exclusion for current benefits received as worker's compensation or disability retirement benefits received in lieu of worker's compensation. The IAFF strongly opposes the elimination of this income exclusion which assists workers who have incurred disability while engaged in public service work. This proposal would prohibit them from maintaining a standard of living comparative to that which they enjoyed prior to incurring their disability. The Internal Revenue Service already taxes benefits received for disability not incurred in the line of duty. It would seem terribly unfair and unjust to penalize individuals who have incurred disabling injuries in the course of performance of duty by eliminating the current tax exempt status.

* The current Administration's proposal has reduced the original recommendations contained in its November tax reform package regarding the taxing of employer paid health and life insurance benefits. However, we continue to have serious reservation about the taxation of any employer paid benefits. First, we would prefer to use the term employer paid benefits instead of the term most often used by the administration - fringe benefits. The use of the term fringe benefits, while referring to employer sponsored plans, enormously understates the importance of these plans which provide basic health security for employees and their families in all income brackets and are available to the vast majority of Americans. Let us start by eliminating any thought that employer paid benefits are only availabe to a few Americans. Preliminary data released by the Employee Benefit Research Institute shows that

approximately 90% of public sector employees are covered by pension, medical, and insurance programs. Other surveyed industries that have higher employer pension, medical, and insurance plan participation rates include manufacturing, public utilities, real estate, finance, insurance, and communications.

The current tax proposal rationalizes that employees' fringe benefits such as health care leads to over consumption of health services. The Treasury Department noted and I quote "Health care is made much more expensive for all because it is effectively subsidized through the tax system for some. The tax advantage now accorded some fringe benefits causes more of them to be consumed." This logic which is based on the market solution theory argues that if a product cost more the use of it will naturally decrease. While some economist may not argue with this logic, it must be remembered that many economist have never scored high marks on compassion and equity. In the area of health care the major cost is surgery, which obviously no one can avoid or predict. Simply put, health care is a vital necessity. Those who have good plans should not be penalized through our tax system. Rather, those who do not provide the basic plans should be encouraged to do so.

Section 301 of the new proposal requires an employee with a spouse or a dependent to add $300 to his or her tax liability. An estimated $15 billion dollars will be raised by such taxes by 1990. Yet, realistically this proposal must be viewed for what it is - a wolf in sheep's clothing. If an employee's health benefits are taxed today, tomorrow those benefits will be taxed to a greater extent and taxation of other benefits such as the contributions made by employers into employees retirement programs will soon follow suit. Ultimately, the original objective of Congress to extend basic services to millions of Americans will be circumvented. If monies which are currently directed toward employee benefit program plans are taxed as income, younger workers will not be inclined or encouraged to allow those funds to be used in providing basic health, life and retirement security. They may foolishly choose to take those funds in direct compensation rather than plan for the future. Should this take place how long will it be before the Federal Government and other levels of government will be looked upon to provide essential health care that individuals no longer have provided for themselves.

* Section 4.05 of the Administration's proposal would repeal the current income averaging provision provided for individuals whose income varies widely from year to year. Currently, if an individual's income for the taxable year exceeds 140% of average income for the 3 preceeding years the effective tax rate applicable to such excess income generally will be the rate that would apply to 1/4 of the averageable income. The elimination of this provision would hurt many public workers who are forced to relocate and change employment. For example: many public workers prior to their retirement vesting date are allowed or required to withdraw their pension contributions plus interest in a lump sum distribution. These individuals, without the income averaging rule, would be required to pay income tax on that amount in addition to their annual salary. Therefore, the IAFF would recommend that the Congress modify the

current proposal which would repeal income averaging to allow averaging to apply to lump sum distributions derived from defined benefit or defined contribution retirement plans.

We understand that you will be hearing from hundreds of special interest groups asking you to modify current proposals contained in the President's plan or other tax reform measures so as to minimize the effect on their own concerns. We additionally understand that to maintain credibility in this legislative process, an effort should be made by each interest group which is asking for modification of provisions which would eliminate or reduce revenues to offer suggestions as to how those revenues can be replaced. In that spirit the International Association of Fire Fighters would like to suggest a few ways in which this Committee can shape a tax reform package that will move more decisively toward tax justice without the revenue loss of the President's current proposal and without increasing the taxes of a vast majority of working Americans.

To bring true fairness to the overall package we recommend further responsibility be placed on the corporate side of the income tax ledger. We strongly suggest that the fundamental factor in constructing a balanced and equitable tax system is for corporations to pay their fair share of Federal taxes. In 1981, corporate tax cuts helped to generate enormous revenue losses, created a new industry around the buying, selling, and leasing of tax write-offs, and opened gaping inequities among companies and industries and between individuals and corporations. Today, corporate America generates approximately 6% to 8% of total Federal revenues, down from approximately 25% only 30 years ago. The IAFF urges the Committee to consider the following suggestions:

* Reduce the top corporate tax limit cut from the present 46% to the proposed 33%. It is our understanding from the Treasury Department that each point reduction represents $2 to $3 billion dollars yearly in revenue. Therefore, a cut less than the current one-third recommended would reduce top corporate tax rates and still add possibly another $10 to $12 billion dollars in revenues.

* Strengthen the corporate minimum tax. After many years of open scandal over the fact that hundreds of major corporations whose profits total billions of dollars pay little or no taxes, a fair but effective minimum tax could raise several billion dollars more than the President's proposal which raises less than $1 billion.

* Reject the Administration's proposal for a 10% deduction for corporate dividends. This provision merely provides this nation's corporations with roughly $6 billion tax windfall for doing something that they would do in any event, distribute dividends to their shareholders. These shareholders in large part are the public pension plans we represent.

*Curb tax privileges of the oil and gas industry. We note with interest that the Treasury's November recommendation would have trimmed many unnecessary special preferences for the oil and gas industry increasing federal revenues by nearly $10 billion per year. The President's current proposal trims oil tax reform by one-tenth of that amount. Enacting Treasury's original recommendations appears to be fair and just.

In conclusion, Mr. Chairman, it is not the position nor the responsibility of the National Conference to understand the tax implications for all industries and sectors of our economy. We do, however, have the responsibility for protecting and enhancing the retirement income security of our membership and provides sufficient and effect fire protection throughout the United States. The Administration's current proposals, which we identified early in our testimony would severely harm not only our public membership but also middle income workers who rely on their retirement plans to enjoy some dignity and security during their retirement years. While reviewing these retirement related proposals, we ask that the Committee not view them only as a way for eliminating possible abuse and misuse by high income and salaried individuals, but view them as an integral component of the total compensation package for millions of public workers who have served their states, localities and nation during their years of public service. We stand ready to answer any questions the Committee may have and look forward to working with you and your staff in developing a fair, equitable and simplified reform package.

STATEMENT OF MOE BILLER, PRESIDENT, AMERICAN POSTAL WORKERS UNION, AFL-CIO, WASHINGTON, DC

Mr. BILLER. Mr. Chairman, Senator Moynihan, I am representing the 325,000 members of the American Postal Workers Union. I appreciate your invitation to testify here.

I have already provided the committee with copies of my full statement and attachment.

Postal workers, like most middle class working Americans, were delighted when they first heard that there might be tax reform. Like everyone else, we dreamed up images of our taxes going down, our tax forms magically disappearing, and we were delighted in the image of wealthy tax-avoiders being hauled in by their earlobes to pay their fair share.

Only the very wealthy would disagree with the father of a distinguished member of this committee whose advice was to "soak the rich." Unfortunately, the more we look at tax reform as it seems to be taking shape, the more it appears to be an exercise to soak the middle class. While some upper income tax loopholes have been reduced, lowering the top rate for individuals from 50 to 35 percent when it was 70 percent just 4 years ago can hardly be called "soaking the rich."

Not everything is bad about the President's plan. It does provide significant relief from taxes for the taxpayers with the lowest incomes. Unfortunately, however, it was this President who pushed an unfair tax bill through the Congress in 1981 and created much of the unfairness that exists today in addition to the enormous deficit.

In 1981 he provided tax cuts for the rich, while letting inflation erode the little guy's personal exemption and earned income. Now in 1985, he is providing the biggest tax cuts for the rich again; but this time he claims it is fair because he is also doing something for the lower income taxpayer. He is trying to take credit for solving a problem that, with the consent of Congress and this committee, he created some 4 years ago.

Both Houses of Congress have been debating the projected budget deficits, and I am appalled that the entire revenue side of the budget deficit has kind of been left out of this year's debate. I am very skeptical, given the problems Congress and the White House are having over the deficit, that tax reform will truly mean a reduction of taxes for the middle class. Individual rates probably won't be cut. If deficit reduction isn't successfully accomplished, rate reductions could be delayed or, if enacted, raised once again in the next Congress.

The American Postal Workers Union will support tax reform if tax reform really means tax equity. Mr. Chairman, we believe sufficient evidence exists to make the judgment that the President's tax reform plan fails a fairness and equity test.

In order that it be better understood how the Reagan tax reform proposal will affect postal workers, the American Postal Workers Union has undertaken two study efforts. First, we have prepared 144-case studies comparing the taxes paid by typical postal workers under the proposed plan versus current law. Second, we are currently conducting a survey of postal workers to learn how many are single filers versus married, how many itemize, and other characteristics. We believe these studies will help our members understand the effects of the Reagan plan on individual taxpayers and will enable us to work with this committee in developing true tax reform. With your permission, we have shown you several samples of our case studies and submit a summary of the study for the record.

The two most outstanding revelations from the case studies are, first, that the Reagan proposal is biased in favor of one-earner two-parent families and against two-earner families. In fact, all the cases examined that itemize their deductions, married couples with one wage earner were the only tax filers that would benefit from reduced taxes. All other itemizing tax filers in these case studies would pay more taxes under the proposed plan.

The second effects? Those postal workers who now itemize deductions, they will pay more taxes under the Reagan plan, and the main reason is the proposed elimination of deductions for State and local taxes. Only a handful of the cases with itemized deductions would be better off due to other provisions of the Reagan plan.

The study revealed that two-parent families with one wage earner would benefit greatly from the proposed increase in deductions for contributions for spousal IRA's and the increase in the personal exemption.

Our case studies show that the bias against two-earner families, particularly those with children, is attributable to the combination of the proposals to repeal the two-earner deduction and convert the childcare credit to a deduction. The childcare credit, which offsets the amount of taxes due, provides the most relief to low-income tax families.

To sum up the study, taxpayers who are typical of our members will come out very differently under the Reagan plan, according to how much income they have and how many people earn it. The one-earner family with children will gain a great deal, but other will not. Among the two-earner families, those with the more modest incomes will be disadvantaged compared to those who are better off financially.

Finally, with your permission I would like to submit at a later date a further analysis that includes the results of our survey. The answers should tell us whether or not our suspicions are confirmed that the Reagan plan is not even a good plan to begin tax reform let alone finish it.

This concludes my statement, Mr. Chairman. I would be happy to answer any questions. And I also subscribe, the same as the others, against the taxation of what we call "fringe benefits," health and so on.

I remember very well a mayor in New York City, probably the most progressive of all time, Mr. LaGuardia, imposed a 0.5-cent sales tax because it was essential. Today they are 8½ percent, or whatever it is.

Thank you very much.

Mr. CHAIRMAN. Thank you, Mr. Biller.

[The statement of Mr. Biller follows:]

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Testimony of Moe Biller,
President

American Postal Workers Union, AFL-CIO

before the

Committee on Finance,
United States Senate

on Tax Reform

July 24, 1985

Testimony of Moe Biller, President
American Postal Workers Union, AFL-CIO

INTRODUCTION

Mr. Chairman, I am Moe Biller, President of the American Postal Workers Union. I appreciate your invitation to testify today on tax reform in general and specifically on the President's proposal.

The American Postal Workers Union represents over 325,000 postal workers in every State, Territory, Congressional District and local jurisdiction in the Nation. The American Postal Workers are a cross-section of solid, hard-working, middle class American workers. The APWU is matched by few organizations of national scope in its geographical distribution. Our members are a part of, and in constant daily contact with, the working middle-class backbone of America.

I. THE PUSH FOR TAX REFORM

A. The Tax Reform Bandwagon

The American Postal Workers are **very wary** of the current discussion of tax reform. We're wary, because we've had direct experience over the last four years with what "reform" can mean to an anti-worker, pro-wealthy class, political leadership. For us, "reform" has meant destruction of postal and federal pay and benefits.

Everyone seems to agree that there should be reform of our federal tax system. We all dreamed up images of our taxes going down, our tax forms magically disappearing, and we have delighted in images of wealthy tax avoiders being hauled in by their ear lobes to pay their fair share. After the initial blush of enthusiasm when people get beyond those early dreams, however, they start thinking of what tax reform really means. The President has said he wants to make it fair and simple. On the issue of fairness, he has said he is putting out the word to big corporations and wealthy tax avoiders now thumbing their noses at the tax collector that "the free ride is over." The President has stated that those individuals and companies must pay their fair share to make the tax system fair for the average taxpayer.

To accomplish simplicity, he has held out the vague promise of a return-free system.

I hope, Mr. Chairman, that you realize that if you start with the President's plan, you are going to have a very, very tough job to make tax reform fair, and I doubt if you will gain much simplicity.

B. Tax Relief for the Poor

The President's plan is not without some good features. A few can be selected out of his plan, improved, and used in a Senate bill.

The most promising feature of the tax reform plan submitted by the President is that it provides significant relief from taxes for the taxpayers with the lowest incomes.

By increasing the zero bracket amount (standard deduction), the personal exemption, and the earned income credit (a special tax break for low-income working families), the President's plan would raise the tax threshold -- the income level at which tax liability begins -- above the poverty line for married couples and for families with children, thus relieving families living in poverty of the obligation to pay federal income taxes. In addition, the Reagan plan would index the earned income credit, so as to prevent the value of the credit from gradually being eroded by inflation.

Although these measures would provide urgently needed relief and lift an unfair tax burden from an estimated 2.5 million poor people, there are several problems with showering praise in the direction of this Administration.

First, this relief would not extend to poor single individuals. Rather , the tax threshold for single people would remain below the poverty line under the President's proposal. In 1986 (assuming the Reagan plan were fully in effect), an individual living alone at the poverty level would be required to pay income taxes of $135 on an income of $5,800.

Second, although President Reagan is treating this tax relief for the poor as his grand accomplishment, let us keep this all in perspective. In reality his plan would do little more than bring poor people back to where they were when he took office in terms of their tax liabilities. In 1980, the tax threshold for a family of four was above the poverty line -- in other words, families living in poverty would have paid no income tax. Since that time, however, the tax threshold has been allowed to gradually drift below the poverty line, requiring millions of poor people to pay taxes for the first time in years.

Although poor families would be better off under the Reagan program than they are under current law, they would still be worse off than they were in the late 1970s. According to an analysis by the Center on Budget and Policy Priorities, the total federal tax burden (income and payroll taxes) on a family of four living at the poverty level would be 4.9% in 1986 under the Reagan plan, compared to 4.0% in 1978. If the same family had income 25% above poverty, the combined federal tax burden would be 9.6% in 1986 under the Reagan plan, compared to 7.8% in 1978.

By basing his low-income relief primarily on increases in the personal exemption and the zero bracket amount, the President's plan would provide an even greater tax give-away to the most wealthy. Greater emphasis should be placed on the earned income credit as a means of tax relief to the working poor.

It was this President who pushed an unfair tax bill through Congress in 1981 and created much of the unfairness that he speaks against today. In 1981, he provided tax cuts for the rich while letting inflation erode the little guy's personal exemption and earned income credit. Now in 1985, he's providing the biggest tax cuts for the rich again, but this time he claims it's "fair" because he's also doing something for the lower-income taxpayer. When it comes to fairness in taxation, the President is worse than a "Ronnie-come-lately" -- he's trying to take credit for solving a problem that, with the consent of Congress and this committee, he created four years ago!

C. Postal Worker Support for Tax Reform

The American Postal Workers will support tax reform, if tax reform truly means tax equity and tax simplification. We will not support "reform" if it means wealthy individuals and companies will continue to pay the current low effective rates. We will not support "reform" if it means retaining the plethora of economy-distorting tax shelters and distorted business incentives. And we will not support tax "reform" if it continues to place government on the current starvation diet which, with the exception of defense spending, is reducing the necessary functions of government to an anemic state.

D. Tax Reform and the Deficit

Both Houses of Congress have been engaged in lengthy debate for at least the last two years over the current stream of projected deficits. I am appalled that the entire revenue side of the budget deficit has been left out of this year's debate.

I am very skeptical, given the problems Congress and the White House are having over the deficit. Individual rates probably won't be cut. If deficit reduction isn't successfully accomplished, rate reductions will be delayed or, if enacted, raised once again in the next Congress. Pity Reagan's successor who will have to pick up the pieces. We were all told to appreciate the Reagan tax cuts. The rich certainly appreciated; they laughed all the way to the bank. Unfortunately, the Reagan tax cuts broke the government's bank -- the Treasury.

The American Postal Workers Union will not support tax "reform" if it adds to the deficit.

As an overall tax reform bill and, indeed, even as a starting point, the President's plan falls short.

II. INDIVIDUAL TAXES

A. Case Studies

To better understand how President Reagan's tax reform proposals will affect Postal Workers, the American Postal Worker's Union has prepared 144 case studies comparing the taxes paid by individuals under the proposed plan versus current law. The cases simulated the effects of the changes on single filers, heads of households and joint filers with and without children at three salary levels that are typical for postal workers and many middle-class, working Americans. Each of the cases was examined with and without investment income, Individual Retirement Account (IRA) contributions and itemized deductions.

The most outstanding revelation from the case studies is the bias of the Reagan proposal in favor of one-earner, two-parent families and the bias against two-earner families. In fact, of all the cases examined that itemize their deductions, married couples with one wage earner were the only tax filers that would benefit from reduced taxes under the Reagan proposals. All other itemizing tax filers in the case studies (married couples with two wage earners, single filers and single heads of household) would pay more taxes under the proposed plan.

The study revealed that two-parent families with one wage earner would benefit greatly from the proposed increase in the deduction for contributions to spousal IRAs and the increase in the personal exemptions. For example, a family with $14,369 in income from one wage earner, with two children, would pay $71, or

14 percent less, in taxes under the President's plan. Without the children and the additional $1,840 in exemptions allowed for them under the Reagan proposal, a couple earning $14,569 would pay $78 less in taxes if they made contributions to an IRA. Without the IRA contributions, that couple would pay $231 more in taxes under Reagan than current law.

In contrast, each of the two-earner, two-child families in the study that itemize deductions would pay more taxes, ranging from 20 to 1,000 percent more, under the Reagan plan. This bias against two-earner families, particularly those with children, is attributed to the combination of the proposals to repeal the two-earner deduction and convert the child care credit to a deduction. The child care credit, which offsets the amount of taxes due, provides the most relief to lower-income families. A child care deduction is of greater benefit to higher-income families because they can deduct a larger percentage at higher tax rates. Consequently, as evidenced in the case studies, the lower-paid families ($21,854) with two children, no investments and no IRA contributions would be required to pay an additional 593 percent in taxes; the same type of family with $46,846 of income would pay only 18 percent more in taxes under the Reagan plan.

To sum up this study, taxpayers who are typical of our members will come out very differently under the Reagan plan according to how much income they have and how many people earn it. The one-earner family with children will gain a great deal, but others will not. Among the two-earner families, those with the more modest incomes will be disadvantaged compared to those who are better off financially.

B. Survey of APWU Membership

We are in the process of conducting a survey of our members to learn how many are single filers, versus married, how many itemize, and other characteristics. With your permission, Mr. Chairman, we would like to submit the results of this survey and compare the results to our case studies at a later date before the hearing record is closed. Our case studies already reveal that most two-earner households in the postal worker salary ranges would have tax increases under Reagan's plan. Our survey should reveal how actual postal worker families will fair under the major proposals in the Reagan plan.

C. Health Benefit Tax

There is one feature of the proposal that I can speak about today without waiting for survey results. I strongly oppose the proposal to tax the health insurance benefits of working people. The President's plan will increase virtually every working person's taxable income by either $120 or $300 a year depending on whether the person has individual or family health insurance coverage. I believe that fringe benefits should not be treated as taxable income because they are not available to the employee for discretionary spending. Instead, they are part of the employment package for which employees have negotiated to meet critical personal needs. To reduce the worth of these benefits, and to do it in a way that does not differentiate between the rich and the poor or between the full coverage health plan and the very limited plan, amounts to an attack on the basic welfare of lower- and middle-income families. This proposed tax is very regressive. It would tax 5 times the percentage of income of someone at 125 percent of the poverty level compared to someone at $100,000.

For postal and federal employees, this additional tax on health benefits would come at a time when the Federal Employees Health Benefits program (FEHBP) has just taken a four-year beating at the hands of this anti-public worker administration. Postal workers lost, on average, over $830 each year due to administrative manipulation of the FEHBP program in 1982, 1983 and 1984.

This is the sort of "reform" we have experienced from this administration. I urge this Committee to draw from our skepticism as you examine this administration's tax proposals.

D. Taxing Fringes--Health and Retirement

Taxing fringes will mean a curtailment of certain activities Congress has in the past chosen as means to foster improvements for employed people. Retirement and health are two of those areas. They are both being attacked by the President's plan. I've already mentioned the widely discussed health "floor" tax. Less widely discussed is the provision to levy an excise tax of 20 percent on all pension distributions before age 59 1/2 from employer-sponsored retirement plans.

This is not good employment policy, especially for jobs involving long employment in high stress work or heavy labor. After 37 years working at a job involving constant, intense manual labor, at say age 57, many physically burned-out long-time workers would be caught in the decision of risking their health for another couple of years or facing the 20% penalty.

E. Taxing Unemployment and Injured Workers Compensation

Several other proposals trouble us greatly. The President's plan would tax many benefits that affect the middle- and lower-income Americans. The plan would repeal exemption from taxation of all unemployment compensation (currently taxed for individuals whose incomes exceed $12,000; couples exceeding $18,000). It would also tax workers compensation for job-related injuries.

F. Fairness and Upper-Income Tax Breaks

At the same time the President is shifting major burdens to segments of the middle class, the President's proposal leaves several areas of tax avoidance relatively untouched. The increased limitations on deductions for business meals and special tax breaks for oil and gas are minor. The Reagan plan also continues the special tax treatment for capital gains --

perhaps the most important tax break for upper-income individuals. Although the President's plan would cut the capital gains exclusion (that is, the portion of capital gains not taxed) from 60% to 50%, the reduction in overall tax rates would mean that the maximum tax on capital gains income would actually fall -- from the present 20% to 17.5%.

Particularly disturbing are the tax benefits directed through tax-rate reductions to the very wealthy. The Reagan tax cuts begin to rise sharply in the $100,000 to $200,000 range, climbing to an average tax cut of $686 for that group compared to $149 for those in the $20,000 to $30,000 range. For those earning over $200,000, however, the average tax cut is a phenomenal $9,254. This tax cut for the wealthy does not occur simply because they pay the most taxes, but also because they receive significantly bigger rate reductions than do middle-income taxpayers. The average percentage tax cut for those over $200,000 is 10.7 percent, compared to 8.7 percent for those between $20,000 to $30,000, and 6.6 percent for those between $30,000 and $50,000. The problem of high-income individuals paying little or nothing in taxes is by now a familiar one and is often cited as one of the major reasons why tax reform is needed. Add this to the average of $30,000 a year or more in tax reductions for individuals earning over $200,000 since the 1981 rate reductions and expanded tax avoidance devices. At the same time, the Treasury estimated that in 1983, 9,000 people with incomes greater than $250,000 paid no taxes. These cuts for the wealthy should make anyone question the President's stated goal of fairness.

G. Fairness and Families

President Reagan also stresses that his proposal would greatly increase tax fairness for families. In fact, he claims that the plan is the "strongest pro-family initiative in postwar history."

Increased fairness for families under the Reagan plan would come largely from the proposed increase in the personal exemption. Since one exemption may be taken for each family member, this increase would provide particular relief for families with dependent children. As the President and others have pointed out, this exemption has not kept pace with inflation over the past several decades.

However, beyond the increase in the personal exemption, the Reagan plan does not spread its relief equally among all families. Some would do much better than others. Generally, upper-income families and families which can afford to have one parent at home would tend to gain more than single-parent families or families where both parents work. In fact, as revealed in the APWU case studies many families will be worse off under the President's plan than under current law as a result of the proposed changes in the credit for child care and the proposed repeal of the two-earner deduction.

H. The Marriage Penalty

An aspect of the Reagan tax plan likely to have an adverse effect on many families is the proposed repeal of the two-earner deduction that is currently available to help offset the marriage penalty. This marriage penalty arises because of the tax system's progressive rate structure, which often causes two married people to pay taxes at a higher rate on their combined income than either would pay on their separate incomes if they were single.

The size of this marriage penalty varies depending on income levels and the division of income between the spouses. It is clear that a significant marriage penalty will continue under the Reagan proposal for many couples.

For example, consider two single people each having taxable income of $25,000. Under the rate structure proposed by the President, each would pay a tax of $4,015, for a combined total of $8,030. If they marry and file a joint return, however, their tax would be $9,000 -- $970 more than the combined total they paid when they were single. (If the Reagan plan retained the two-earner deduction in its present form, this married couple would pay taxes totaling $8,375, thus reducing -- but not completely eliminating -- the marriage penalty.)

Clearly, repeal of the two-earner deduction will result in higher taxes for these families and contribute to causing some families to pay more taxes under the Reagan plan than they would under current law.

I. Child Care Credit

In addition, President Reagan proposes to convert the existing credit for dependent care expenses into a tax deduction, thereby transferring much of the benefits from low-income families to upper-income families.

This change in the child care allowance from a credit to a deduction is likely to produce significant losses for many lower-income taxpayers and significant gains for upper-income taxpayers with child care expenses. This transfer would occur partially because credits are inherently more valuable than deductions at low income levels (while the reverse is true at high incomes), and partially because the present credit is specifically directed toward those with lower incomes by a formula which reduces the percentage amount of the credit as income rises. In some cases, lower-income families could end up facing a tax increase under the Reagan program, largely as a result of this change in the child care credit.

J. State and Local Deduction

In your review of the individual tax proposals, I urge the Committee to investigate thoroughly the President's proposal to eliminate the deduction for state and local taxes. The President argues that the dollar value of these deductions goes mainly to taxpayers with incomes over $50,000 and that taxpayers in 15 states are being subsidized by those in the other 35. But you have to look at the individual taxpayer and ask yourself how the loss of this deduction will affect him or her.

The President's own data show that nearly 6 million families with income below $30,000 now take the deduction and another 11 million between $30,000 and $50,000 take it. So it does benefit many middle-income families.

With respect to subsidies among states, taxpayers in the high-tax states also pay more in federal taxes than they get back in benefits and services, and that fact has to be taken into account.

It should also be noted that many of the 35 states President Reagan says are subsidizing New York and California also have high marginal tax rates but, because of small populations or low per capita incomes, don't derive a large benefit in the total value of the deductions statewide. The taxpayers in these states who do deduct will feel the effects nonetheless if they lose their deductions. For example, Montana applies a 10-percent tax rate to taxable income between $24,000 and $42,000. North Carolina has a 7-percent income tax rate above $10,000, and West Virginia has a 10.5-percent rate on income between $26,000 and $32,000. If taxpayers in these states lose the right to deduct the state income tax, they will in effect face a sizeable increase in the net cost of their state taxes.

As you review this issue, don't be misled by Reagan rhetoric about a few high-tax states---people in all the states will be affected and need to be considered.

III. CORPORATE TAXES

A. Decline in Corporate Taxes

The decline of corporate taxes over the last four years was engineered by the current Administration and it has been phenomenal.

According to the Joint Committee on Taxation, corporate taxes have fallen by 14 to 18 percent since 1980. According to a February 1985 report by the Congressional Budget Office, the average effective corporate tax rate (after all the specific corporate tax breaks are accounted for) has been cut in half since 1980. Along with individual tax shelters and a lower rate for top income earners, the burden for funding the government and the enormous defense buildup has been shifted to average wage earners.

B. Corporations Paying No Taxes

In a recent study of 250 U. S. companies provided to Ways and Means by the Citizens for Tax Justice, we learned that the median tax rate for those 250 companies has reached a miniscule 8.7 percent. Over one-half of those companies had at least one year in the period from 1981 to 1983 in which they either paid no federal taxes or received refundable credits. Over a fourth of those companies paid no taxes at all from 1981 to 1983. We've heard ample testimony of where these tax refunds have gone--GE, Boeing, Dow Chemical, Tenneco. Even the firm headed by that great, self-styled waste-fighter, Peter Grace, received $12.5 million in tax refunds on a profit of $684.1 million from 1982-1983. Like cats caught in the canary's cage, some are now scurrying around and saying "we're sorry we took the money and ran." They hope they can keep the heat off by advocating a minimum corporate tax fix, and they hope that the members of this committee and your colleagues on the other side of the Hill will buy their rhetoric and the President's rhetoric and keep hands off the basic corporate tax. The telling figures are, however, that in the 1950's and 1960's corporate income taxes paid for a quarter of federal spending, excluding Social Security which is self-financing. In 1984, corporate income taxes paid less than one-eleventh of federal spending.

If you are looking for some place to raise revenues, look there.

CONCLUSION

In closing, I urge the Committee to come up with a tax bill that is fair to the working people of this country and that does not increase the budgetary pressures we are now under. We must restore the trust of the average taxpayer that federal revenue will not be squandered once again through tax breaks for wealthy corporations and individuals.

Thank you, Mr. Chairman, for this opportunity to testify today.

The **Chairman**. Mr. Shanker, correct me if I am wrong on these statistics—I think I am roughly right—that nationwide, 66 percent of the taxpayers don't itemize, although many of those who do not itemize also don't pay any taxes. In Oregon it is about 60 percent who do not itemize. Senator Moynihan says in New York it is about 56 percent who do not itemize; although two-thirds of those who do itemize pay the bulk of the taxes.

To those who don't itemize, what difference does it make to them whether you can or cannot deduct State and local taxes when it comes to voting on a local tax issue? They may vote for or against it, but the itemization issue wouldn't make any difference, would it?

Mr. **Shanker**. Well. I think you might have a differential turnout of voters on these issues. Only about 15 percent of the voters turn out for local school board elections on those votes. I think you would need a better picture of what the turnout is. But there is no doubt in my mind that there would be an effect on it.

It might very well be that the people who don't do the paying don't do as much voting.

The **Chairman**. I think you probably well could be right if you are talking about special elections, not held on a normal primary or general election day where you can expect a large turnout regardless.

Mr. **Shanker**. Well, many of your funding elections and school board elections are exactly that type. As a matter of fact, 98 percent of them are not partisan elections; they take place at a different time—the same voting booths frequently, but brought out at different times. So I think you are dealing with a very separate politic here.

The **Chairman**. You are, and the most motivated voters turn out in those particular kinds of elections. They may be generally good, decent citizens who turn out for all special elections, or they be motivated about that particular special election; but I would be willing to bet anything that they are probably not a cross-section of the average voter or the average income earner.

Mr. **Shanker**. I think you get two groups that would be very highly represented. I think you get parents who are interested in providing, maintaining, or improving services, and I think you get taxpayers who are worried about the burden of taxes. Those are the two groups that would be over represented. Then you get a smattering of people who vote in the public interest, or have a general interest, or some view of what the school board ought to be. But I think those two groups would be the groups that turn out for the most part.

The **Chairman**. A second statistic, and assuming the Treasury's estimates are right, I am not for a moment going to argue that one way or the other; the joint committee is doing some estimates of their own, also. But over 5 years, if Treasury is right, individuals get tax cuts of $132 billion, business get tax increases of $118 billion. The reason I am inclined to think that is close to right is that business doesn't like it. They have some real misgivings about this bill. The bulk of those individual tax cuts do not go to the very wealthy. Percentagewise thay get a larger than average tax cut, but because there are relatively few wealthy, the quantity of money distributed, as you might expect, among the middle-income taxpayer. It has to be; that is where the bulk of the money is.

You don't think when a voter would go to the polls that he or she thinks, "Well, I have lost the right to deduct my State tax or my property tax; but on the other hand, my Federal taxes have been cut. So I can afford now to pay 100 cents on the dollar for local taxes instead of 72 percent, because my Federal taxes have been cut."

Mr. **Shanker**. I don't think most of them will, especially, as Mr. Biller pointed out, and I agree with it, I think in terms of numbers the broad number of people who turn out—I mean those same small number who get the large amounts, also, not the majority of taxpayers they represent, or voters; they represent a very small percentage of voters—I think that the impact here is what effect it has on the broad range of middle-class people. They are the ones who are going to come out in large numbers to vote. And I agree with the analysis that was given; I think that with exception of the family with a single breadwinner that the others are adversely affected, and they are going to be looking at ways of cutting back, because they are going to be hurt by this provision, and they are going to be looking for some way of recapturing some of that money. They can't really capture it very well in a sales tax; they have to buy certain things. They are going to have to do that. But the one place where you can do it very easily, where there are votes almost every year in most of the districts—I don't know what other public services would survive in this country if we had to vote for them every year; I don't know if we would have a country left if we had to have a referendum every year. But in most of these districts the public gets in a very direct way—that's the one place where they can say No, where they can express their anger about all their other taxes—a very sensitive area, and that's the school tax.

The **Chairman**. And yet it is ironic, on the average, that they don't say no to those running for Federal office. They return most of us to office year-in and year-out, even though we are the ones who pass on these decisions, levy the biggest bite of taxation on them. And if they don't like it, they could say no to us, but for some reason they don't.

Mr. **Shanker**. They have a broader range of issues here. Down there, there is just one single place they can do something. And let's face it, everybody gets some benefit, direct and indirect, out of various things that the Federal Government does. I think everybody gets some benefit out of what a local school system does, too, but many people don't realize it. When their own children are in school, they feel it is a benefit to them. And then you have the civic-minded person who understands that education is not just an individual good. But you have quite a few people who, once their children are out, or if they have no children at all, they are just—you have got to start with them as an opposition group frequently.

The **Chairman**. That's fair enough. It is unfortunate. Almost everybody realizes the advantage of Mr. Schaitberger's union—they put out fires. And you can just as well have one whether you have children or not. But I know what you mean in terms of those whose children are gone. They supported the schools and belonged to the PTA, and did everything while the kids were there, and then change their views later.

Senator Moynihan.

Senator **Moynihan**. Mr. Chairman, first I want to thank the panel for their first-rate testimony. You only gave it in capsule, but you gave us real data and real numbers, and they certainly appealed to me.

I would like to make a general statement first, if I can. In all truth, if one were to ask me what I think the most important effect this bill would have, it would be on public education. In there there is an exact calculation which you can make, and Mr. Shanker has it in his testimony. Assuming a 28 percent marginal rate across the country—a CRS figure—eliminating State and local tax deductibility would increase the after tax price of local education by about 40 percent. A big tax increase? Incredible. And it is kind of curious. There are some 15,400 school districts in the country. They are a form of Government—unique, I think, to America. I don't know any other country that has them. they have taxing power. And there are more units of this Government than any other kind of government. They take on the most important responsibility of government, other than national defense, which is education. They do it in a nonpartisan way; there is not a Republican or Democrat elected in any of those 15,000 boards. It is the most public regarding, quietest unit of government, and it would really be ravaged by this proposal. And it has no tradition of being here in Washington looking after itself, because it doesn't get involved with Washington, and Washington doesn't put up its money. And, boy, I think we are letting them down.

I might say that there is not much interest in this. I mean, I don't think we have 15 Senators on this State and local thing.

It would help, to be frank, if we had a bishop over there saying, "Don't take away our tax credits"; but that opportunity came and went.

Let me say a couple of things. I heard both Mr. Lucy in that very lucid and capable testimony, and I guess Al Shanker mentioned it also, that the notion that there is going to be a big "interstate subsidy effect of the deductibility" is really greatly overstated. There is no doubt that there have been many States in the union which, by keeping their public services low, have thought they were serving their economic advantage. They haven't. I mean, look where technological innovations come from: the highest tax States, which have the best schools, the best universities.

And as this sinks in, people in those low tax States realize they are going to have to raise taxes. But if they lose they will find they are not going to be able to raise taxes and when, after three generations of not educating their children, they realize that an uneducated workforce doesn't really produce much in the way of economic growth it will be too late.

You are all national organizations. Do you perceive that in some of these States and municipalities that have stayed behind, they are beginning to sense this isn't really in their interest? Mr. Lucy?

Mr. LUCY. Well, Senator, I don't think there is any question. I think that basically there are two questions of policy involved here, and that is whether or not we want our local communities, both cities, counties, and States, to be a strong economic area. And certainly business or the corporate community will not locate, it seems to me, anywhere where the infrastructure or the facilities needed to have a sound operation don't exist. And certainly if the question of the deductibility will reduce the potential of an income at the local level for providing these amenities, that sort of squashes, it seems to me, any real competitive edge that a community might have.

Second, I don't think it is any secret that the Tax Code has been used in the past and will possibly be used in the future to promote issues of national concern. The high tax States, so to speak, are really in effect paying for things that are important on a national basis; they are important to the constituents of those States. I think it is just sound policy to allow for certain kinds of conditions that exist in certain areas—not by any action of the State but simply by virtue of vast numbers of people living in areas which require special kinds of programs.

I would also say that the States where the greatest per-capita per-citizen is expended is not where you would traditionally think they are; there are other States benefiting far more from the tax system.

Senator MOYNIHAN. As, for example, Alaska and Wyoming.

Mr. LUCY. Well, Oklahoma isn't doing bad; but Alaska and Wyoming are typical.

Senator MOYNIHAN. Yes.

Mr. LUCY. And if we look at New York, the State that I am sure the Senator is aware of, which is some 22 to 25 percent below those in terms——

Senator MOYNIHAN. That's right, as you are expert on.

Mr. CHAIRMAN. If I could just ask one more question, just to Mr. Geiger?

The CHAIRMAN. Yes.

Senator MOYNIHAN. On your page 5, you say that "the range of direct Federal funding for elementary and secondary education in the States is from 3.2 percent to more than 17 percent." Now, are you saying that in some States the Federal Government puts up as much as 17 percent?

Mr. GEIGER. That is true.

Senator **Moynihan**. Would you offhand know that's true?

Mr. **Geiger**. Sure; it is basically the Southern States, Mississippi and Louisiana and so on. The Southern States basically get more of their money from the Federal Government than do the Northeast States.

Senator **Moynihan**. So what they are asking is to keep that 17 percent? I know in the case of New York it is 3.

Mr. **Geiger**. Yes; I am aware of that.

Senator **Moynihan**. And so, we are going to have to give up our deductibility of our high taxes, because we pay our own way, to the advantage of those people who don't pay their own way, where the Federal Government in a sense compensates for low levels of State effort. Right?

Mr. **Geiger**. There isn't any question that one of the reasons the whole Federal Government got into the public education in the late fifties and early sixties was so those who have could help those who don't have.

Senator **Moynihan**. I was there.

Mr. **Geiger**. Let me go back to one of the questions that was asked earlier, because it poses an interesting dilemma, this whole thing.

In 1983, in Indianapolis, when we did what we called the show and tell time with the Commission on Education Excellence report, Secretary Bell had a national conference. President Reagan came to that conference and went into great lengths to talk about the fact that public education in this country was basically a State and a local responsibility.

Governor Orr of Indiana—and if you get out the transcript, you can read it—went into great lengths to talk about the fact that public education was basically a local responsibility. If you look at Indiana, you will see that in 1972—I believe the year was—Indiana froze property taxes in that State.

Now, that is a dilemma that we all have to work with and live with; but public education is a responsibility of local, of State, and of national, and if we go back to dealing with the deductibility of the local and the State, not only are you saying it is more a responsibility of the local and the State but you are taking away that privilege that we have of paying those taxes. That is a problem that we have to wrestle with at all three levels.

Senator **Moynihan**. Thank you, Mr. Chairman.

The **Chairman**. Senator Bradley.

Senator **Bradley**. Thank you very much, Mr. Chairman, and I apologize for not being here earlier, but I had one of these Intelligence Committee meetings which, as the Senator from New York, the former vice chairman, knows eat away incessant hours of listening to information that you are not able to tell anyone. [Laughter.]

The **Chairman**. There should be more such committees.

Senator **Bradley**. That is true.

I apologize for not being here earlier. But I do find the testimony that I have read extremely helpful.

I must say I was struck by a point that Mr. Kirkland made in his testimony that I think is particularly relevant to this whole tax debate. It was on page 8, where he is talking about the fact, that the President has proposed increasing the personal exemptions.

He said:

> The President's plan relies heavily on increases in the personal exemption to remove the poor from the tax roles and offset the removal of many middle class deductions and exclusions. The value of the personal exemption, however, is considerably higher for wealthy individuals.

And then he goes on to make the point,

> A fairer system would ensure that the personal exemption is worth the same to all individuals, regardless of income.

Now, is that something, broadly, that each of you also support?

Mr. **Shanker**. We would certainly support that, no question about it.

Mr. **Lucy**. That would be the same for us.

Mr. **Geiger**. Yes.

Mr. **Schaitberger**. Yes.

Mr. **Biller**. Yes.

Senator **Bradley**. I think that is a very interesting idea. Personal exemptions and deductions are both worth more to upper income individuals in higher tax brackets than they are to middle income individuals. I think that Mr. Kirkland's suggestion on how to handle the exemption might be equally instructive for a whole variety of other issues. And I think it is very significant that he would make that statement.

Let me ask the panel, for our deliberations: I have looked at all of this, and I agree with Senator Moynihan that there is a lot of valuable information in here. In general terms I would like to ask you whether you agree with a few basic principles.

Do you agree that any tax reform should not increase the deficit? Maybe you can just go down the line and say yes or no.

Mr. **Geiger**. Yes.

Mr. **Shanker**. Yes.

Mr. **Lucy**. Yes.

Mr. **Schaitberger**. Yes.

Mr. **Biller**. Yes.

Mr. **Shanker**. I think it should decrease it.

Senator **Bradley**. OK. That is a strong point of view. OK.

Do you agree that any tax reform should not—and I underline not—increase the relative tax burden on middle- and low-income people?

Mr. **Geiger**. Yes.

Mr. **Shanker**. Yes.

Mr. **Lucy**. Yes.

Mr. **Schaitberger**. Yes.

Mr. **Biller**. Yes.

Senator **Bradley**. Do you agree that any tax reform proposal should give the lowest tax rate to the greatest number of people? And to do this, the "greatest number of people" are middle- and low-income people, so they have to get a much lower tax rate.

Mr. **Shanker**. Yes.

Mr. **Schaitberger**. Yes.

Senator **Moynihan**. Three out of three?

Senator **Bradley**. I thank the panel very much.

Mr. **Lucy**. I am not sure all the panel is finished. Your question leaves me somewhat confused, because I am not clear as to whether or not in each one of these questions you have posed we are speaking of meeting the revenue needs of the country as a whole.

Senator **Bradley**. No, no. My point in asking the question is, everyone comes in and talks about a portion of a total plan. The point is, obviously, every group has specific interests. But the real question is: What is the effect of the total plan after it is implemented? And the question is, should the effect of the total plan not increase the deficit? Everyone agrees. Should it not increase the relative tax burden on middle- and low-income people? Everybody agrees. Should it have the lowest possible rates for the greatest number of people? Everybody agrees. That is the effect.

Mr. **Lucy**. But I think it has some other dimensions that have to be looked at aside from the personal impact of tax policy on the individual: The question of whether or not we are going to have viable communities in relationship to that; whether or not enough revenue will be generated, not solely for the Federal Government and not solely for the middle levels of Government but enough generated to meet whatever the priorities of each level of Government happen to be.

We think, as we said in our presentation, that there have got to be about three principles upon which a tax program or a reform program is premised, and that is: fairness, and that it raise an adequate level of revenues. In that context it may well be that the burden will shift one way more so than the other. It is difficult to address, as a flat yes or no, unless we agree on some of the other premises.

If we are saying we are going to have adequate education, adequate police and fire protection, adequate public services and infrastruture, I think you will find there are those who are willing to pay a bit more if we are meeting those priorities.

Senator **Bradley**. I don't want to eliminate the State and local tax deduction, either.

Mr. **Shanker**. Senator Bradley, what you are saying is that the answers to those three questions are not enough to give us a decision as to whether we would support a tax program.

Senator **Bradley**. Absolutely.

Mr. **Biller**. May I ask your panel a question, Mr. Chairman?

The **Chairman**. Go right ahead.

Mr. **Biller**. How would you feel about really getting those corporations that been getting their rump on taxes in to pay taxes? I thought about getting them here by their earlobes; I hope I can really get them in.

Senator **Bradley**. You want to know how I feel about it? I think they ought to pay their full share.

Mr. **Biller**. I am just quizzing your panel.

Senator **Bradley**. I mean, this is probably one of the unique moments of congressional history, where the panel is asking the committee a question.

Mr. **Biller**. That is why I asked permission, Senator. [Laughter.]

Senator **Bradley**. I understand. Well, I would certainly say yes.

Senator **Moynihan**. Let me say to you, I had this bill in in the last Congress, and it was the real estate. We went in the backroom and took a vote on it and lost 10 to 9. Then Senator Dole said, "OK, then we raise the depreciation for buildings 20 years." And it ended up 18 at the conference. But we put the bill back in.

I think we are going to get it. The administration is for a higher minimum rate than we are, as a matter of fact. That I think will happen in this Congress.

The Chairman. I think we are going to get an effective corporate minimum and individual tax. Whether or not we get a tax reform bill, I think we are going to get that.

Senator Bradley. I might just say, the real question is how you get that. If you get real tax reform, you get an effective corporate minimum tax to boot. In my view there are three problems with the current system: One is that some people and companies don't pay any tax, and some people and companies pay too much, and the thing is so complicated nobody can understand it. But you have got to address all three of these problems. And that is possible.

Mr. Geiger. But I think Mr. Kirkland addressed that earlier, and I think Bill Lucy addressed that a little bit. I think we still at some point have to face up to the fact that in 1981, when we were all told that you can give a 25-percent tax break, and increase defense spending, and balance the budget—you can't do all three of those.

Senator Bradley. I voted against it.

Mr. Geiger. We are now learning that you can't.

The Chairman. We are adjourned, gentlemen. Thank you very, very much.

Senator Moynihan. Mr. Chairman, I thank you for having put together an absolutely first-rate morning, and the staff who did it.

The Chairman. Thank you.

[Whereupon, at 12:15 p.m., the hearing was concluded.]

[By direction of the chairman the following communication was made a part of the hearing record:]

IMPLICATIONS OF IMPLEMENTING THE PRESIDENT'S TAX REFORM PLAN ON AMERICAN AGRICULTURE

JULY 24, 1985

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INTRODUCTION AND SUMMARY

Overview of Methodology

Wharton maintains detailed models of agricultural markets and of the U.S. economy which are used regularly to produce baseline forecasts and to quantify the implications of changes in baseline conditions. In preparing this analysis of the implications of the President's tax reform plan for the agricultural sector and the U.S. economy, Wharton's Long-Term Model was used first to determine the effects that the tax plan would have on the aggregate U.S. economy. The outputs of this first-step analysis were used to determine the changes in the relevant inputs into Wharton's Agriculture Market Models. These inputs include interest rates, prices for goods and services purchased by the agriculture sector from the rest-of-the-economy, and real personal disposable income. The Agriculture Market Models were then solved to determine the effects of the President's tax plan on the U.S. agriculture sector. The tax plan would affect the agricultural sector directly via the changes in the tax codes applying to agriculture and indirectly through the induced changes in interest rates, prices, and income. Finally, the Long-Term Model was resolved over the 1986-93 period, incorporating both the predicted changes in the agriculture sector as determined by the Agriculture Market Models and the changes in the tax laws indicated by the President's tax reform plan.

The President's Tax Reform Proposal Implies Higher Costs and Lower Income for the Agriculture Sector

Implementing the President's tax reform plan would raise the cost of funds to agriculture. The cost of capital to agriculture, measured by the user cost of capital, would increase by as much as 19.8 percent in the wake of implementing the tax plan. Capital costs would rise due to the elimination of the investment tax credit and accelerated depreciation provisions of the current tax code. Eliminating cash-basis accounting for certain agricultural enterprises and requiring capitalization of certain expenses related to multiperiod investments would further increase the cost of capital to agriculture. Finally, limitations on interest cost deductability would severely limit the use of limited partnerships as a source of cost-effective equity capital to the agriculture sector as well as to other sectors such as real estate. Infusions of equity financing are critical given the already high debt-to-equity ratio in the agriculture sector.

Capital costs in agriculture would also increase due to a rise in interest rates, which would be up by as much as 31 basis points or 4.0 percent, and due to a hike in prices for investment goods, which would rise above baseline levels by as much as 1.3 percent. The increases in capital costs, combined with generally higher prices for the goods and services purchased by the agriculture sector, would raise total production costs in agriculture by $3.2 billion over the 1986-93 period.

The major direct impacts of the higher production costs would fall upon livestock producers, resulting in cutbacks in herd size during the three years following implementation of the President's tax reform plan. Cattle on feed, beef breeding stock, dairy herds, pork breeding and feeding operations, and poultry flocks would be affected. Grain-consuming animal units would be reduced by as much as 4.8 million in 1988, and, on average, by 3.8 percent during the 1986-88 period.

The reduction in livestock herd sizes would cut the feed demand for corn and soybeans. Over the 1986-93 period, corn feed demand would be down by 709 million bushels, and single-year demand losses would reach 150 million bushels. Soybean feed demand would be affected by a lesser amount.

Lower feed demand, and the resulting drop in prices for corn and soybeans, would force grain producers to reduce planted acreage. Corn acreage would be reduced on average by 620,000 acres during the 1986-93 period and, in 1992, by as much as 1,930,000 acres. Over the same period, soybean acres would be cut on average by 176,000 acres.

The drop in the number of grain-consuming animal units and the subsequent cuts in grain production would combine to reduce farm output by $9.2 billion (1985 dollars) over the 1986-93 period. Higher production costs, lower grain prices, and reduced output would combine to cut farm income over the 1986-93 period by $10.3 billion.

Jobs Would Be Lost in Agriculture

The fall in agriculture output and farm income would reduce the number of jobs directly in agriculture by as much as 10,000 during the 1986-93 period. These job losses would include both farm workers and farm owners. The large drop in farm income would raise the farm failure rate given that many farmers already are in a very shaky financial condition. The negative effect of the job and income losses in agriculture would also spill over into other businesses in the farm communities.

Investment in Agriculture Would Be Cut Sharply

Reduced output and income in the agriculture sector, combined with the higher capital costs produced by the President's tax proposal, would lead to sharp cutbacks in agricultural sector investment. In real terms, agriculture sector investment would drop by as much as 11.0 percent. Over the 1986-93 period, agricultural sector investment would be reduced by $5.8 billion (1985 dollars) or by 5.1 percent below baseline levels.

Food Prices Would Rise, Putting a Burden on the Poor and Elderly

Average meat prices would be higher, despite increased marketing of non-fed beef, if the President's tax plan were implemented. Beef prices would increase during the 1987-89 period; these higher beef prices would shift meat demand toward pork and poultry, thereby pulling pork and poultry prices up by essentially the same percentage. Overall livestock prices would increase by an average of 5.0 percent during the 1987-89 period. These higher meat prices, combined with a generally higher rate of inflation, would cause the consumer price index for food to rise by more than the overall price level.

The elderly and poor are affected much more severely by a rise in food prices than is a typical family. As of the most recently available survey data (the 1980-1981 Consumer Expenditure Diary Survey, Bureau of Labor Statistics, U.S. Department of Labor), the average family of four had an average annual income of $20,225 and spent 17.9 percent ($3,623) on food. The same survey indicates that almost 11 percent of all families had an income of less than $5,000. This group of poorest families had an average annual income of only $2,609 and spent 53.2 percent ($1,387) on food. Higher food prices penalize this group severely.

The Presidents' Tax Reform Proposal Would Stimulate Consumer Spending at the Expense of Business Investment

The President's tax reform proposal would reduce effective personal income tax rates but would raise the effective corporate tax rate. As a result, consumer spending would be stimulated while business investment would be retarded. Over the 1986-93 period, consumer spending on average would be increased by 1.1 percent, while business fixed investment would be reduced on average by 2.0 percent. At the end of the period, consumer spending would be sliding back down toward baseline levels, while investment spending would continue to fall further below baseline levels. Consumer spending would peak at 1.3 percent above baseline levels and then fall back to 1.0 percent above the baseline path by 1993, while investment would drop to 2.4 percent below its baseline path at the end of the period.

Higher consumer spending initially would produce a higher level of real GNP, but real GNP would fall back to just above its baseline level by 1993 as the continued declines in investment would offset the consumption gains. The sustained lower levels of business investment would reduce the economy's growth potential beyond the period of this analysis by reducing the capital stock per worker. Short-term gains in consumption would be earned at the expense of longer-term productivity and growth.

Lower Investment Implies Reduced Labor Productivity and Higher Prices

The President's tax plan would produce a consistently lower and diverging level of business investment from 1986 to 1993. By the end of this period, labor productivity would be 0.4 percent below baseline levels due to the reduction in capital equipment available per employee. This reduction in labor productivity would be translated into higher prices. By 1993, the GNP deflator, the broadest published price measure, would be 1.0 percent above its baseline value and would be diverging from its baseline path.

The President's Tax Plan Would Lead to a Worsening of the Trade Balance

Higher U.S. consumer spending, lower U.S. investment, and higher U.S. prices following the implementation of the President's tax plan would lead to a worsening of the already heavily negative U.S. trade balance. By 1993, the cumulative U.S. trade deficit on current account would be increased by $27.4 billion.

The President's Tax Plan Would Raise the U.S. Federal Debt Substantially

The President's tax plan would not be revenue neutral but, instead, would lead to an immediate and longer-term shortfall in net revenues. Between 1986 and 1990, the federal debt would increase by $49.5 billion dollars which is substantially larger than the $11.5 billion shortfall conceded by the Administration (The President's Tax Proposals to the Congress for Fairness, Growth, and Simplicity, May 1985, p. 461). The net revenue shortfall would continue after 1990, and the federal debt would climb to $73.0 billion above baseline levels by 1993.

A COMPARISON OF THE PRESIDENT'S TAX REFORM PLAN AND TREASURY I

This study is an update of an earlier Wharton analysis of the implications of tax reform for the U.S. agricultural sector (Implications of Implementing the Treasury's Tax Reform on American Agriculture, April 30, 1985). The differences between the impacts obtained in the analysis presented here and in the results obtained earlier are due primarily to the changes in the proposed tax reforms. Some slight differences may result form the use of a more recent U.S. forecast as the baseline for the analysis. The current study uses Wharton's Long-Term Forecast, June 1985 as the baseline while the earlier analysis used a forecast prepared in December 1984 as the baseline.

The Two Proposals Are Very Similar

The President's Tax Reform Proposal,(Administration I), eliminates many of the more serious oversights of the initial Treasury proposal (Treasury I). Also, some of the more controversial aspects of the initial proposal, such as indexing of interest cost and income, have been eliminated. However, the President's proposals are qualitatively the same as Treasury I, insofar as:

- the tax base is broadened while tax rates are lowered;
- personal taxes are cut on average; and
- corporate taxes are raised on average

The impacts on the U.S. economy of Administration I and Treasury I also are estimated to be similar. Based on simulations with Wharton's Long-Term Model of the U.S. economy, the implications of implementing Administration I would be that:

- Consumer spending would climb above current-law baseline levels;

- Spending by business on plant and equipment would fall below current law baseline levels;

- Construction of residential housing, particularly multifamily dwelling units, and commercial structures would drop relative to current-law baseline levels; and

- Real output (GNP) initially would be slightly higher due to higher consumer spending but the fall in business and residential investment would quickly force GNP back to baseline levels.

Administration I attempts to provide a somewhat more favorable climate for investment than did Treasury I, primarily by substituting CCRS for RCRS. The net result when compared to the situation under current law, however, would be to make investment less attractive by raising the effective rate of taxation on investment income. The situation would be made substantially worse during the 1986-90 period due to the proposed tax on "excess depreciation" which would raise the effective tax rate on business income.

General Objectives of Tax Reform

The general objectives of the President's Tax Reform Proposal are:

- to simplify the tax system
- to broaden the tax base while reducing tax rates
- to reduce personal taxation
- to increase corporate taxation.

It is far from clear that the President's proposal would simplify the tax code. The tax base would broadened for both personal and corporate (business) taxes, and the marginal tax rates would be cut for both persons and corporations. The net impact of base broadening and rate reduction would differ, however, for persons and corporations. The effective tax rate on gross income would be reduced for persons while it would be increased for corporations.

Personal Tax Changes

The reductions in personal tax collections would be due primarily to three major changes:

- Reductions in the marginal rates
- Increase in the value of the personal exemption
- Increase in the zero bracket amount

The base broadening changes for personal taxes would include:

- Elimination of the deductibility of state and local tax payments
- Repeal second-earner deduction
- Tax a portion of health insurance
- Eliminate income averaging
- Limit the deductability of interest expenses
- Extend the "at risk" rule to include real estate
- Repeal "tax abuse" provisions

The elimination of the deductibility of state and local tax payments is by far the most important change from the perspective of dollar gain to the Treasury.

Proposed Changes In Corporate and Business Taxes

The two changes which would act to reduce corporate tax payments are:

- Reduction in corporate tax rates
- Deductibility of 10% of dividend payments

The progressivity of corporate tax rates would be maintained and the maximum rate would be cut. The former feature would have been eliminated under the Treasury I proposal.

Increases in corporate and other business enterprise taxes would stem from the following:

- Repeal of the investment tax credit
- Change from ACRS to CCRS depreciation for tax purposes
- Recapture of ACRS windfall
- Require capitalization of more costs in cases of multiperiod production and other income measurement changes
- Limit use of cash basis accounting
- Revise taxation of financial institutions
- Eliminate tax free status of IDB's
- Institute a per country tax credit limitation
- Curtail tax shelters

The proposed change in the method of computing depreciation for tax purposes, from ACRS to CCRS, may be seen as a net improvement by many businesses. The problem in determining how this change would be perceived stems from not knowing what discount rate a business would apply to a future stream of depreciation. CCRS would lengthen the tax lives of equipment and structures but would index the undepreciated cost base for inflation. As a result, a greater dollar amount of depreciation would be claimed over the life of an asset under CCRS than under ACRS. The additional depreciation under CCRS, however, would occur after several years. Assuming a 5 percent inflation rate and a 4 percent real discount rate (or a 9 percent nominal discount rate), CCRS would provide a higher discounted present value than does ACRS, for all asset classes. Higher inflation rates would make CCRS more attractive relative to ACRS, but a higher real discount rate would make CCRS less attractive relative to ACRS.

The net effect of all the corporate and other business tax changes would be to raise the tax rate on business. Elimination of the investment tax credit would raise the cost of investment in equipment. These factors, in conjunction with the induced higher inflation and interest rates would reduce business investment.

Provisions of the Proposed Tax Code Which Could Raise Business Costs, Particularly for Agriculture

The Treasury's tax reform plan would require that preproductive period expenses be capitalized for any animal or plant which had a preproductive period of 2 years or longer. This provision would extend the principles now applied to fruit and nut orchards and to vineyards to encompass, presumably, beef breeding operations, dairy operations, and the growing of timber. The requirement that preproductive period expenses be capitalized would increase the after-tax costs of beef operations, dairy operations, and timber operations.

The use of cash method accounting also would be restricted under the Treasury's tax reform plan. Large agricultural enterprises would not be permitted to use cash-accounting methods. While most agricultural enterprises have gross receipts less than the limit specified in the Treasury's proposal, certain types of large agricultural operations, such as beef feed lots, would be hurt financially. If agricultural enterprises were required to shift from cash to accrual method accounting, after-tax operating costs would be increased during the 5-year transition period from the cash method to the accrual method. After the transition period, the after-tax costs would be slightly higher because production costs increase with inflation. New entrants or existing operators who expand would continue to face higher costs for the new or expanded operations.

Eliminating the cash flow method of accounting will result in cash flow problems for some agricultural and many business service businesses. The increased tax costs experienced by these businesses are apt to be reflected in higher service prices. The President's tax proposal would increase tax costs of the affected business by $500 million in 1986 and by $1.1 million per year from 1987 through 1990. Farms which were required to change from the cash method to the accrual method due to implementing the President's plan would be especially hard hit. Farmers switching would have to adjust income for accounts receivable and accounts payable, as would other businesses, and also would have to increase reported income due to the initial use of inventory methods.

The President's proposal would increase the tax liabilities of farmers during the transition period to a greater degree than nonfarmers. If two taxpayers had identical cash method incomes, the farmer would bear a far greater burden in changing to the accrual method than would the nonfarmer. Because of the higher tax liabilities, the farmer also would have greater problems in financing any increased cash outflows needed to pay the increased tax liabilities.

The limitation in personal interest cost deductability to $5000 (other than interest paid on a home mortgage) would severely limit the viability of limited partnerships as a means of cost effective tax-sheltered equity financing for agriculture, forestry, rental housing, commercial real estate, and extractive industries. High income individuals could partially circumvent the interest cost deductability limitation by adjusting their financial asset portfolio to guarantee a financial income stream as an offset against the interest losses generated by limited partnerships. Limited partnerships, however, have been used by upper middle income individuals who probably would be unable to use these methods to circumvent the changes in the tax code.

Some of the industries which now use limited partnerships to raise equity capital, including the agriculture, rental housing, and mining industries, are weak financially, have high debt-to-equity ratios, and would have to pay a large premium for access to non-tax-sheltered equity financing. The alternative to allowing this form of tax-sheltered equity financing to continue may be to pay direct subsidies to insure that adequate rental housing is available, that strategic minerals are produced, and that the farm failures do not become excessive.

CALCULATION OF THE MACROECONOMIC IMPACTS OF THE PRESIDENT'S TAX REFORM PLAN

Changes to Wharton's Long-Term Model Inputs

The President's tax reform plan proposes a total overhaul of our tax system. It is impossible to explicitly account for all the changes, but we have accounted for the effects of all the major changes. The input changes described below have been subjected to critical outside review and have been amended since our initial analysis of the tax plan to incorporate the refinements suggested by these reviewers.

Inputting Personal Tax Law Changes

The Wharton Long-Term Model has 15 tax brackets for joint returns. The exemption is set at $2000 per person and is indexed to inflation, which is roughly 4.7% per year. The average value of deductions on a standard return, the zero bracket amount, is set to $4000 and is indexed. The average value of deductions for an itemized return is reduced by $2389 from 1987 to 1994. This value is calculated as the necessary reduction in the value of itemized deductions due to the elimination of state and local tax deductibility. The proportion of standard (unitemized) returns out of total returns is set to 66.7%; this is higher than the average under the current-law baseline.

The marginal personal tax rates are set to the relevant rate--15%, 25% or 35%--for all income brackets. Where the brackets do not correspond, the midpoint of the two tax rates is used. All tax brackets are indexed to inflation. The add-factor for personal tax collections is changed to take into account all other personal tax changes (both increases and decreases) implied by the president's proposal. Appendix C, pp. 453-61 of The President's Tax Proposals to the Congress for Fairness, Growth, and Simplicity, was used in making the add-factor calculations.

The effective tax rate for homeowners, used in the user cost of single starts, is reduced from 38% to 30%--halfway between the 25% and 35% marginal personal tax rates. The effective tax rate for landowners, used in the user cost of multiple-unit starts, is reduced from 50% to 33%, the marginal tax rate for corporations.

Inputting Business Tax Law Changes

The investment tax credit level and the industrial investment tax credit rates are all set to 0.0. The effective corporate tax rates are adjusted to reflect the new marginal rates, the 10% dividend deduction, the recapture of the rate differential on accelerated depreciation, the changes in the taxation of foreign income and the change in the pattern of depreciation. The following pattern results for the effective corporate tax rates:

1986	1987	1988	1989	1990	1991	1992	1993	1994
36%	39%	37%	34%	32%	31%	30%	29%	28%

From 1986 to 1989, the effective rate is greater than the marginal rate because of the recapture clause. From 1990 onward, the dividend deduction proposal and the new form of depreciation schedules result in a declining effective rate. Though the depreciation schedule normally enters the model through the tax base, the new form of depreciation, which is very beneficial to long-lived capital goods, results in a benefit to business that is best handled through the effective tax rate in the Long-Term Model.

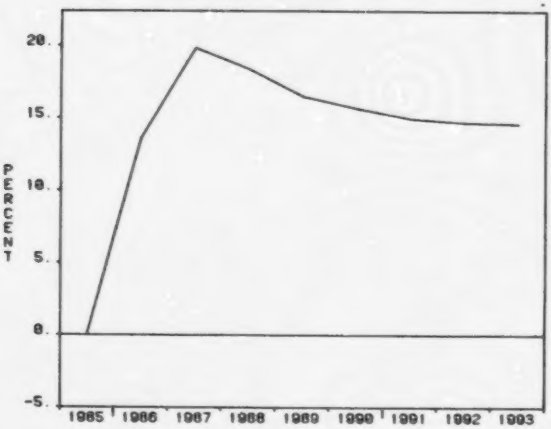
The corporate capital adjustment allowance is reduced from 1986 to 1990, and after 1990 it returns slowly to the baseline assumption. This again reflects the beneficial return of CCRS to long-lived capital assets. The tax lives of the industries are set at the midpoint between the baseline tax lives and the tax lives consistent with the Treasury I proposal. The add-factor for corporate tax collections is set to 0.0 to reflect the elimination of many tax shelters.

OVERVIEW OF KEY MACROECONOMIC RESULTS USED AS INPUTS INTC THE AGRICULTURE MARKET MODELS

The most important changes in the macroeconomic inputs into Wharton's Agricultural Market Models are cost related. Agricultural sector capital costs, measured by the user cost of capital, would increase dramatically. This capital cost measure would jump above its baseline value by 13.6 percent in 1986 and would climb to 19.8 percent above the baseline path in 1988 as shown in Figure 1. In 1993, the agriculture cost of capital remains 14.6 percent above the baseline. This figure and all subsequent figures show changes from baseline levels due to implementing the President's tax reform plan. A zero value implies no change from baseline.

FIGURE 1

AGRICULTURAL CAPITAL COSTS UP
(Percent Change From Baseline)

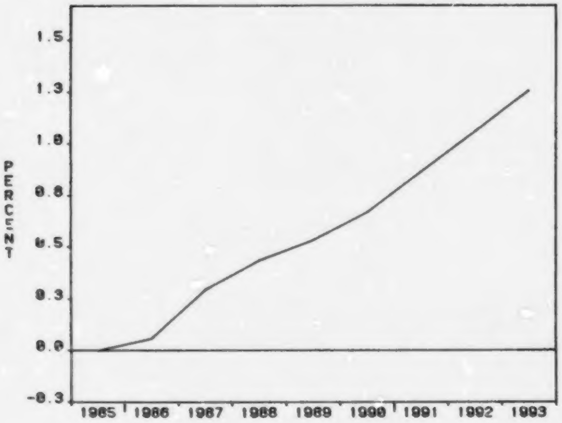


Appendix A presents the percentage change in user cost values in 1993 between the "Baseline" to the "President's Plan" scenario for agriculture and all other industries identified in Wharton's Long-Term Model. The induced changes in capital stock by industry also are shown.

Most of the initial increase in agricultural sector capital costs would be due to the changes in the business tax rates and rules. After the first year, however, higher inflation and interest rates would contribute to the higher agriculture sector capital costs. As shown in Figure 2, the price of investment goods would rise steadily above its baseline path, reaching, in 1993, a point 1.3 percent above its baseline value. Higher prices would result from a reduction in labor productivity, which, in turn, would result from a reduction in investment per worker.

FIGURE 2

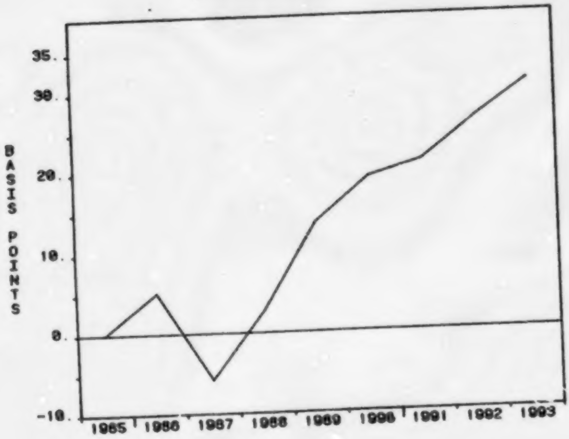
PRICES OF INVESTMENT GOODS RISE
(Percent Change From Baseline)



As displayed in Figure 3, interest rates also would be above baseline levels throughout most of the period as a result of implementing the President's tax reform plan. This result, generated by the Long-Term Model, would be due to slightly higher inflation rates.

FIGURE 3

INTERREST RATES ARE HIGHER
(Change From Baseline)



The proponents of the President's Tax Reform Proposal argue that interest rates should fall because marginal personal tax rates have been cut. While this change should put a downward pressure on interest rates, we believe that other factors would offset this downward pressure and that interest rates would be slightly higher.

On factor contributing to higher interest rates is the increase in the federal government deficit (i.e., the net revenue loss due to the changes in the tax code). The higher level of government borrowing would put an upward pressure on interest rates.

A key concern is the role and posture of the Federal Reserve Board. The Fed has taken a very strong anti-inflationary stand recently and could cause interest rates to rise by restricting the money supply as inflation rates begin to creep upward. The response by the Federal Reserve is, by far, the largest of all effects on interest rates, and the monetary authorities have it in their power to make interest rates go in either direction. We have assumed that the Federal Reserve Board would accomodate some but not all of the increase in nomimal GNP which would result from implementing the President's plan.

Other issues clouding the interest rate change that might result from implementing the tax proposal include the following:

- While the marginal rates for many taxpayers would fall, it may raise the effective marginal rate for the very wealthy who control most assets, and who now take full advantage of tax loopholes. If so, these individuals may seek a higher before-tax rate of return.

- The tax proposal may raise the relative cost of equity financing and increase the use of debt instrument financing.

- The interest rate enters the rental rate (user cost) of capital formation as a proxy for the total cost of all funds to business. The total cost of funds may not be reduced, considering the points above.

- U.S. interest rates are determined, to an extent, in international markets. Since foreigners do not pay U.S. taxes on income earned abroad and funds move freely across the U.S. border, this would offset the downward effects of reduced U.S. tax rates.

- International funds are very volatile. If funds flee the United States (or stop entering the country) because of less favorable tax treatment here, the cost of funds may rise.

- The tax law changes may reduce the marginal propensity to save. If so, this would tend to raise interest rates.

The last point is controversial since a reduced marginal tax rate increases the after-tax return from savings. The lower marginal tax rates, however, also reduce the amount one must save to attain a given future level of income. Therefore, if people are to meet specific future dollar requirements (e.g., downpayment on a house, college tuition, or retirement), then a lower marginal rate implies a lower marginal savings rate.

Other inputs from the macroeconomic model into the agricultural models include real personal disposable income and real consumer spending on food. Since the President's tax reform plan would reduce personal taxes, real personal disposable income would increase, which, in turn, would lead to an increase in consumer spending on food. The "Baseline" and "President's Plan" values for all the key inputs are shown in Appendix C. Real personal disposable income would climb above baseline levels by as much as 1.5 percent in 1990, but then fall back toward baseline levels to reach a point, in 1993, 0.9 percent above its baseline. Real expenditures on food would increase by at most 1.1 percent above baseline levels.

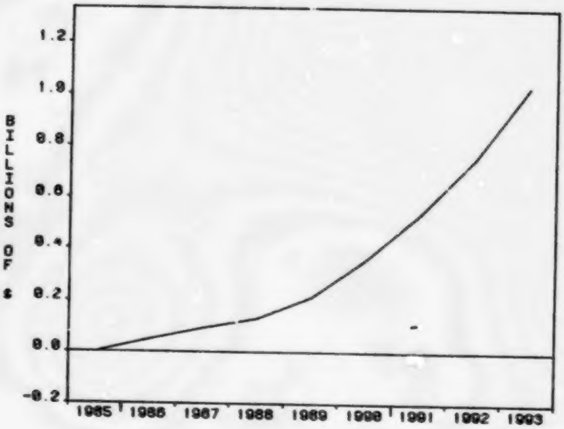
ANALYSIS OF AGRICULTURAL SECTOR IMPACTS OF THE PRESIDENT'S TAX REFORM PLAN

Costs, Production, and Income

Farm production expenses would increase directly as a result of the higher capital costs, increased inflation rates, higher interest rates, and higher effective business tax rates. Over the 1986-93 period, total farm production expenses would be $3.2 billion higher under the President's tax plan. Most of this increase occurs during the second half of the period as farm production expenses track the increases in inflation and interest rates, which would climb substantially during the 1990-93 period. Figure 4 illustrates the increases in farm production expenses over the 1986-93 period.

FIGURE 4

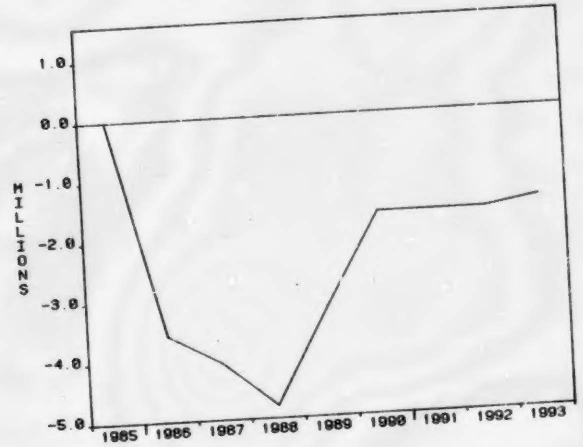
FARM PRODUCTION COSTS INCREASE
(Change From Baseline)



Production costs for livestock producers, particularly beef cattle feeding operations, would rise by a greater percentage than costs for grain producers. Beef feeding operations would be scaled back, resulting in increased marketings of non-fed beef. The cutbacks in beef feeding operations would reduce the demand for feeder cattle, leading to reductions in beef breeding stocks. While beef prices would fall in the very short run due to increased marketings of non-fed beef, these prices would quickly begin to climb due to the drop in the supply of fed beef. As a result, annual average beef prices in 1986 would be unchanged, but prices would rise significantly thereafter. Consumer demand for meat would shift further toward pork and poultry, thereby putting upward pressure on their prices. As pork and poultry prices are pulled upward, pork and poultry production would increase. On average, over the 1987-89 period, livestock prices would increase by 5.0 percent. The net impact on the total livestock herd size, however, would be negative. Grain-consuming animal units--the total number of animals measured in terms of relative consumption where the basis is grain consumed by a producing dairy cow--would fall by 3.6 million units in 1986 relative to baseline levels. As shown in Figure 5, the herd size would decline further during 1987 and 1988, reaching a low point 4.8 million units (4.4 percent) below the baseline. Meat prices would be enough above the baseline levels by 1988 to generate a moderate recovery in the herd size. The total number of grain-consuming animal units would reach, in 1990, a point 1.5 percent below baseline levels and remain below the baseline path by approximately that percentage through 1993.

FIGURE 5

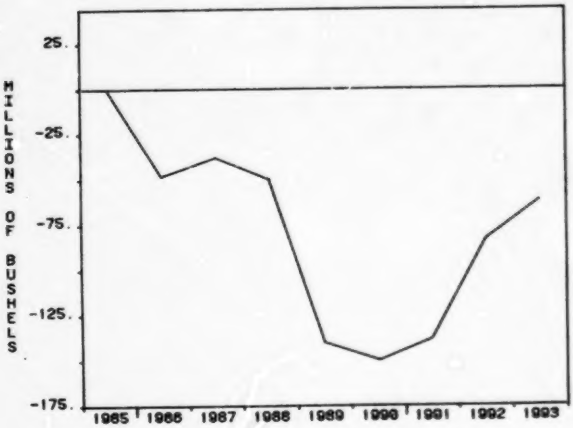
GRAIN-CONSUMING ANIMAL UNITS REDUCED
(Change From Baseline)



Fewer animals, particularly fewer cattle on feed lots, would translate directly into a reduced demand for feed. This demand drop would hit corn demand hardest because corn is the predominant U.S. feed grain. Animal feeding represents the largest category of corn use, averaging about 60 percent of total demand in an average year. Over the 1986-93 period, corn utilized for animal feed would decline by a total of 709 billion bushels. The decline in corn feed demand would follow the liquidation of fed beef herds and end in 1990 as beef price increases provide some stability to the livestock sector. Between 1990 and 1993, feed demand would recover but not to the level of use that existed prior to the imposition of the President's tax reform plan, despite lower corn prices. Figure 6 illustrates the changes in corn feed demand due to implementation of the President's plan.

FIGURE 6

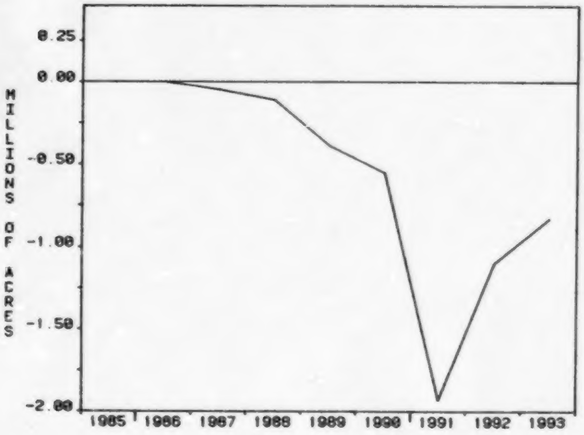
FEED DEMAND FOR CORN IS DOWN
(CHANGE FROM BASELINE)



The combination of lower prices caused by reduced feed demand and higher production costs, which reflect increased taxes, interest rates and input prices, would reduce returns per acre for corn. The lower returns for corn--particularly in comparison with soybeans, where demand is not as diversely affected by the liquidation in the fed beef industry--would cause producers to take advantage of the assured existence of paid diversion crop set-aside programs and would reduce the amount of land planted to corn. Reflecting weak prices and poor returns, total corn acreage planted would be reduced by 620,000 acres over the 1986-93 period. The sharpest declines would occur in 1990 and 1991 as area is cut in order to adjust production to a lower pattern of demand and to avoid excessive stock accumulation. Figure 7 illustrates the impact of the President's tax plan on land area planted to corn.

FIGURE 7

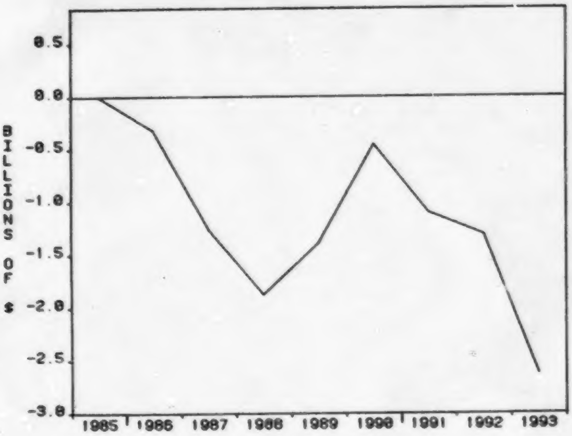
CORN ACREAGE IS CUT BACK
(CHANGE FROM BASELINE)



The reductions in livestock and grain production over the 1986-93 period would translate into a drop in real agricultural sector output of $9.2 billion (1985 dollars). Reduced output combined with lower grain prices would result in a drop in farm cash receipts. Despite reductions in annual herd size and planted area for major grains, farm production expenses would be higher due to increased capital costs, higher taxes, higher interest rates, and higher inflation. As a result, net farm income would fall substantially below baseline levels, as shown in Figure 8. Over the 1986-93 period, the loss of farm income would total $10.3 billion.

FIGURE 8

FARM INCOME DROPS
(Change From Baseline)



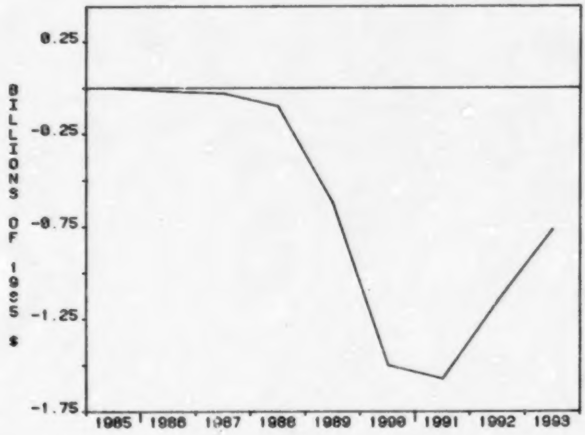
The detailed numerical results underlying the above graphic presentations are presented in Appendix B.

Agriculture Sector Investment

As a result of implementing the President's tax reform plan, agricultural sector investment would be reduced by $5.8 billion (1985 dollars) over the 1986-93 period. As illustrated in Figure 9, investment would drop sharply relative to baseline levels after 1988, dropping to 11.0 percent below the baseline in 1991. Total business investment by all industries would be reduced, over the 1986-93 period, by 2.0 percent relative to baseline levels, but, over the same period, agriculture sector investment would be cut by 5.1 percent. The sharp increase in agriculture capital costs would be a major factor contributing to the decline in the agriculture sector's investment, but the decline would be exacerbated by the declines in farm output and income.

FIGURE 9

REAL AGRICULTURAL SECTOR INVESTMENT IS DOWN
(Change From Baseline)

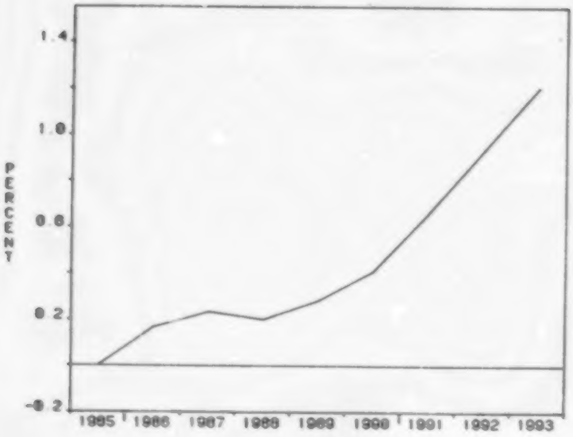


Food Prices

Food prices would increase as a result of higher meat prices and also as a result of a higher general price level. Food prices, measured by the food CPI, would rise steadily above baseline levels if the President's tax reform plan were implemented, as shown in Figure 10. By 1993, food prices would be 1.2 percent above the baseline. In the same year, the overall price level would be 1.0 percent above baseline levels. The larger increase in food prices would be the result of a larger-than-average cost burden being imposed on the agriculture sector by the President's tax plan.

FIGURE 10

FOOD PRICES ARE UP
(Percent Change From Baseline)



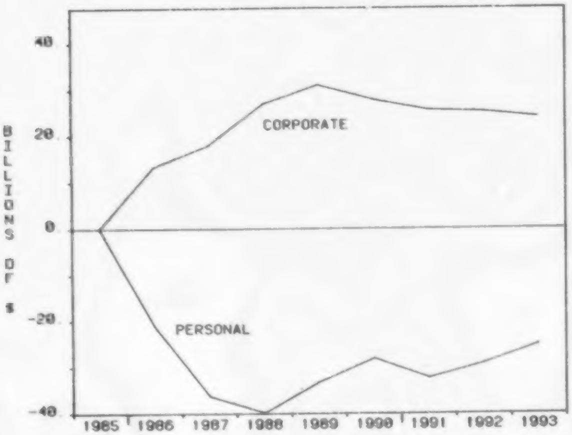
ULTIMATE EFFECTS ON THE U.S. ECONOMY OF IMPLEMENTING THE PRESIDENT'S TAX REFORM PLAN

Corporate Versus Personal Tax Receipt Changes

If the President's tax plan were implemented, taxes on business activity would increase substantially while personal taxes would fall by a greater absolute amount as shown in Figure 11. Corporate tax receipts would rise by as much as 33.3 percent (in 1989 and 1990) relative to the baseline and personal taxes would fall by as much as 8.9 percent (in 1987 and 1988) relative to baseline levels. In dollar terms, personal taxes are reduced over the 1986-90 period by $158.1 billion and, over the same period, corporate taxes are higher by $117.0 billion.

FIGURE 11

CORPORATE TAXES RISE SUBSTANTIALLY BUT BY A LESSER AMOUNT THAN PERSONAL TAXES FALL
(Change From Baseline)



Consumer Spending, Business Investment, and GNP

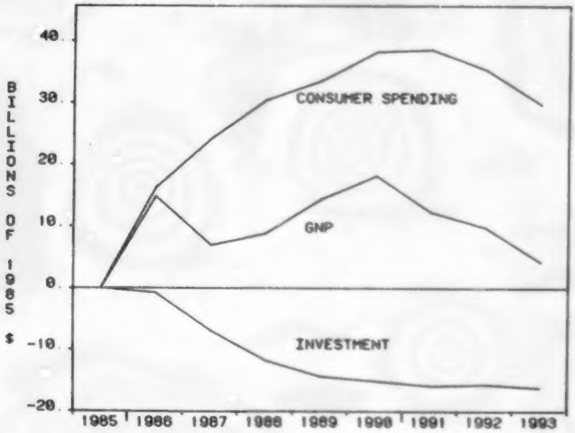
The cut in personal taxes would increase real disposable income, and, as a result, consumers would increase their spending levels. Consumer spending would increase initially by 0.6 percent above baseline levels and climb, by 1990, to a point 1.3 percent above the baseline path. Consumer purchases would then recede toward baseline levels, and, in 1993, would be 1.0 percent above the baseline.

The increase in business taxes would raise the cost of capital to business and reduce business investment. In 1986, business investment would be only 0.4 percent below the baseline, but this difference would widen to 2.6 percent by 1990. On average over the 1986-93 period, business investment would be lower by 2.0 percent, while consumer spending would be 1.1 percent higher if the President's tax plan were implemented.

Figure 12 illustrates the changes in consumer spending, business investment, and GNP which would result from implementing the President's tax proposal. Higher consumer spending would initially increase output (GNP), but the steady erosion of investment spending would drag GNP back down to just above baseline levels by 1993.

FIGURE 12

GNP IS UP BECAUSE CONSUMER SPENDING IS UP,
BUT INVESTMENT IS DOWN
(Change From Baseline)



Productivity and Prices

The sustained lower levels of business investment would reduce the capital equipment available per worker. The reduced availability of capital per worker would cause productivity to fall. By 1993, labor productivity would be 0.4 percent below baseline levels.

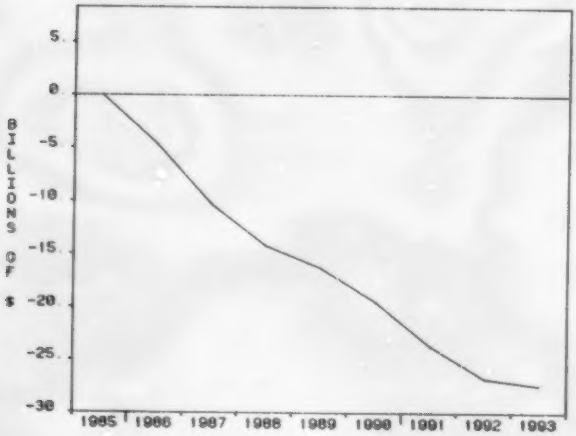
Reduced labor productivity, in turn, would lead to higher unit labor costs and higher price levels. The overall U.S. price level, measured by the price deflator for GNP, would be 1.0 percent above baseline levels by 1993.

U.S. Balance on Current Account

Lower productivity and higher prices would hurt the international competitiveness of U.S. goods. This factor, combined with higher levels of U.S. consumer spending under the President's tax plan, would further increase the U.S. trade deficit. Figure 12 shows the change in the U.S. current account balance which would result from implementing the President's proposal. By 1993, the U.S. net balance would be worse by an accumulated $27.4 billion.

FIGURE 13

CUMULATIVE TRADE BALANCE IS WORSE
(Change From Baseline)

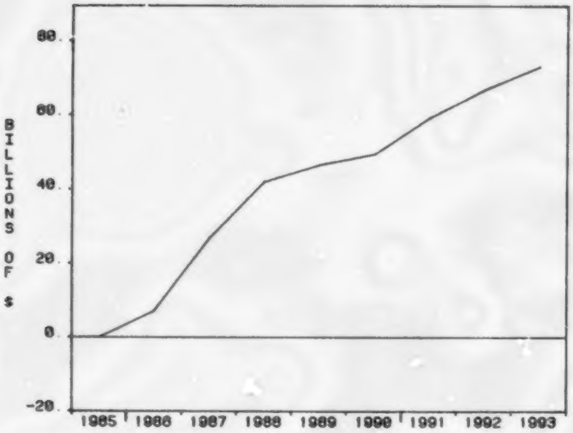


Federal Government Debt

A key difference between the President's tax reform proposal and the initial Treasury proposal is that the President's plan would not be revenue neutral. Instead, the federal debt would be raised significantly due to a reduction in net federal receipts. As shown in Figure 14, the federal debt would increase steadily above baseline levels if the President's plan were implemented. By 1993, the federal debt would be $73.0 billion higher.

FIGURE 14

FEDERAL DEBT IS UP SUBSTANTIALLY
(Change From Baseline)



The detailed numerical results underlying the above presentation are shown in Appendix C.

APPENDIX A

CHANGES IN COST OF CAPITAL AND CAPITAL STOCK FOR ALL INDUSTRIES DUE TO THE PRESIDENT'S TAX REFORM PLAN

TABLE A-1

INCREASE IN THE COST OF CAPITAL IN 1993 BY INDUSTRY
(Percent Difference from Baselines)

Industry	Percent Change
Agriculture	14.6
Mining	9.7
Durable Manufacturing	
Lumber	16.6
Furniture	10.8
Stone, Clay and Glass	15.7
Primary Metals	13.4
Fabricated Metal Products	15.6
Nonelectrical Machinery	12.0
Electrical Machinery	12.4
Motor Vehicles	14.4
Nonauto Transp Eq & Misc Manuf	14.1
Instruments	12.7
Nondurable Manufacturing	
Food and Beverages	12.6
Tobacco	7.2
Textiles	15.3
Apparel	14.0
Paper	17.5
Printing and Publishing	17.6
Chemicals	17.1
Petroleum	10.5
Rubber	16.2
Leather	14.2
Transportation	10.2
Commercial	14.6
Utilities	11.0
Communications	5.9
Total Resid Housing Units	20.6
Owner-Occupied	12.9
Landlord-Owned	44.0
Mobile Homes	11.0

TABLE A-2

REDUCTION IN THE CAPITAL STOCK IN 1993 BY INDUSTRY
(Percent Difference from Baselines)

Industry	Percent Change
All Industries	-1.3
Agriculture	-4.2
Mining	-1.0
Durable Manufacturing	-1.6
Lumber	-0.7
Furniture	-8.7
Stone, Clay and Glass	-2.6
Primary Metals	-2.8
Fabricated Metal Products	-9.0
Nonelectrical Machinery	-1.6
Electrical Machinery	-0.1
Motor Vehicles	-0.6
Nonauto Transp Eq & Misc Manuf	-0.1
Instruments	-0.1
Nondurable Manufacturing	-0.5
Food and Beverages	0.9
Tobacco	0.0
Textiles	-0.2
Apparel	-1.4
Paper	-1.6
Printing and Publishing	-5.3
Chemicals	-0.8
Petroleum	0.2
Rubber	-0.1
Leather	-0.1
Transportation	-7.5
Utilities	0.3
Communications	-0.7
Commercial	-0.8

APPENDIX B

CHANGES IN THE U.S. AGRICULTURE SECTOR DUE TO IMPLEMENTING THE PRESIDENT'S TAX REFORM PLAN

TABLE B-1

GRAIN-CONSUMING ANIMAL UNITS BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

(Million Units)

	Base	Alt	Diff
1986	108.1	104.5	-3.6
1987	107.5	103.4	-4.1
1988	108.2	103.4	-4.8
1989	109.9	106.7	-3.2
1990	110.9	109.2	-1.7
1991	112.8	111.1	-1.7
1992	111.8	110.1	-1.7
1993	114.1	112.6	-1.5

TABLE B-2

LIVESTOCK PRICE INDEX BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

(1953-57 = 1.0)

	Base	Alt	% Diff
1986	2.57	2.57	-
1987	2.37	2.51	5.8%
1988	2.51	2.62	4.5
1989	2.57	2.69	4.6
1990	2.63	2.65	0.8
1991	2.54	2.56	0.8
1992	2.53	2.55	0.7
1993	2.73	2.69	-1.6

TABLE B-3

AREA PLANTED FOR CORN AND SOYBEANS BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

	CORN			SOYBEANS		
	Base	Alt	Diff	Base	Alt	Diff
	(Million Acres)			(Million Acres)		
1986/87	82.00	82.00	---	67.00	67.00	---
1987/88	78.00	77.95	-0.05	67.20	67.20	---
1988/89	76.90	76.79	-0.11	67.80	67.80	---
1989/90	76.30	75.91	-0.39	71.50	71.22	-0.28
1990/91	80.00	79.45	-0.55	71.90	72.12	0.22
1991/92	83.00	81.07	-1.93	73.00	72.70	-0.30
1992/93	83.00	81.90	-1.10	73.00	73.00	---
1993/94	83.50	82.67	-0.83	75.00	73.95	-1.05

TABLE B-4

FEED DEMAND FOR CORN BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

(Million Bushels)

	Base	Alt	Diff
1986/87	4477	4429	-48
1987/88	4351	4313	-38
1988/89	4421	4371	-50
1989/90	4531	4391	-140
1990/91	4710	4560	-150
1991/92	4775	4637	-138
1992/93	4742	4659	-83
1993/94	4818	4753	-62

TABLE B-5

VARIABLE COST OF PRODUCTION FOR CORN AND SOYBEANS BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

	CORN			SOYBEANS		
	Base	Alt	Diff	Base	Alt	Diff
		($/acre)			($/acre)	
1986/87	$182.28	$182.46	$.18	$96.10	$96.11	$.01
1987/88	191.65	191.74	.09	101.60	101.61	.01
1988/89	200.53	201.37	.84	106.84	106.86	.02
1989/90	208.82	210.39	1.57	111.43	112.19	.76
1990/91	217.13	218.53	1.40	116.31	117.01	.70
1991/92	225.39	226.86	1.47	121.32	122.04	.72
1992/93	234.03	237.03	3.00	126.83	128.56	1.73
1993/94	243.50	247.04	3.54	132.48	134.30	1.82

TABLE B-6

IMPACT ON CORN AND SOYBEAN FARM PRICE BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

	CORN			SOYBEANS		
	Base	Alt	Diff	Base	Alt	Diff
		($/bu)			($/bu)	
1986/87	$2.65	$2.52	$-.13	$5.89	$5.82	$-.07
1987/88	2.95	2.75	-.20	6.22	6.18	-.04
1988/89	3.04	2.85	-.19	6.50	6.49	-.01
1989/90	3.09	3.11	.02	6.38	6.58	.20
1990/91	3.27	3.24	-.03	6.71	6.75	.04
1991/92	3.18	3.22	.04	6.78	6.88	.10
1992/93	3.28	3.20	-.08	6.97	6.98	.01
1993/94	3.23	3.16	-.07	6.86	6.97	.11

TABLE B-7

U.S. FARM PRODUCTION EXPENSES
BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

(Billion $)

	Base	Alt	Diff
1986	$154.65	$154.70	$.05
1987	160.08	160.17	.09
1988	165.47	165.60	.13
1989	169.42	169.63	.21
1990	177.42	177.78	.36
1991	183.52	184.06	.54
1992	190.08	190.83	.75
1993	197.73	198.76	1.03

TABLE B-8

U.S. NET FARM INCOME (USDA DEFINITION)
BASELINE AND PRESIDENT'S TAX PLAN ALTERNATIVE

($ Billion)

	Base	Alt	Diff
1986	$25.64	$25.32	$-0.32
1987	24.58	23.32	-1.26
1988	20.04	18.17	-1.87
1989	22.39	21.01	-1.38
1990	25.66	25.21	-0.45
1991	25.93	24.83	-1.10
1992	24.79	23.48	-1.31
1993	29.81	27.19	-2.62

EFFECTS ON THE U.S. ECONOMY
OF IMPLEMENTING THE PRESIDENT'S TAX PLAN

	1986	1987	1988	1989	1990	1991	1992	1993
GROSS NAT PROD (BILL 72 $)								
PRESIDENTS TAX REFORM	1732.4	1783.9	1847.0	1906.4	1915.2	2001.7	2061.7	2113.8
BASELINE	1726.1	1780.9	1843.2	1900.3	1907.4	1996.4	2057.5	2112.0
DIFFERENCE	6.4	3.0	3.8	6.2	7.8	5.3	4.2	1.8
% DIFFERENCE	.4	.2	.2	.3	.4	.3	.2	.1
GNP DEFLATOR (1972=100)								
PRESIDENTS TAX REFORM	242.8	254.4	266.9	280.5	295.3	307.1	320.0	334.5
BASELINE	242.8	254.5	266.9	280.1	294.4	305.6	317.7	331.2
DIFFERENCE	-.1	-.1	.0	.4	.9	1.6	2.3	3.3
% DIFFERENCE	.0	.0	.0	.1	.3	.5	.7	1.0
REAL OUTPUT PER PERSON (THOU 72 $)								
PRESIDENTS TAX REFORM	16.050	16.308	16.583	16.814	16.880	17.185	17.428	17.628
BASELINE	16.014	16.307	16.581	16.809	16.882	17.219	17.479	17.700
DIFFERENCE	.035	.001	.002	.005	-.001	-.034	-.051	-.072
% DIFFERENCE	.220	.007	.010	.032	-.008	-.200	-.295	-.406
FED GOVT DEFICIT (BILL $)								
PRESIDENTS TAX REFORM	-185.5	-198.5	-183.4	-171.1	-176.9	-172.9	-169.8	177.5
BASELINE	-178.4	-178.8	-168.1	-166.7	-173.9	-163.0	-162.1	-171.4
DIFFERENCE	-7.1	-19.7	-15.3	-4.4	-3.0	-9.9	-7.6	-6.0
% DIFFERENCE	4.0	11.0	9.1	2.6	1.7	6.1	4.7	3.5
FED PERS TAX RECEIPTS (BILL $)								
PRESIDENTS TAX REFORM	350.1	369.8	410.1	478.0	552.5	597.9	644.8	696.4
BASELINE	371.0	405.9	450.0	511.2	580.6	630.1	673.9	721.5
DIFFERENCE	-20.9	-36.1	-39.9	-33.2	-28.1	-32.2	-29.1	-25.1
% DIFFERENCE	-5.6	-8.9	-8.9	-6.5	-4.8	-5.1	-4.3	-3.5
FED CORP PROFIT TAXES (BILL $)								
PRESIDENTS TAX REFORM	89.4	102.6	119.1	124.2	111.2	122.1	131.5	134.1
BASELINE	76.1	84.6	92.2	93.2	83.5	96.5	106.3	110.0
DIFFERENCE	13.3	18.0	26.9	31.0	27.8	25.7	25.2	24.0
% DIFFERENCE	17.5	21.2	29.2	33.3	33.3	26.6	23.7	21.9
BALANCE ON CURR ACCOUNT (BILL $)								
PRESIDENTS TAX REFORM	-120.9	-126.1	-118.9	-105.6	-84.7	-107.3	-111.4	-102.0
BASELINE	-116.3	-120.3	-115.0	-103.4	-81.6	-103.1	-108.3	-101.4
DIFFERENCE	-4.6	-5.7	-3.9	-2.1	-3.1	-4.1	-3.2	-.6
% DIFFERENCE	3.9	4.8	3.4	2.0	3.9	4.0	2.9	.6
PRIME COMM PAPER RATE, 6 MO (%)								
PRESIDENTS TAX REFORM	6.55	7.04	8.13	9.02	9.94	7.99	7.75	8.05
BASELINE	6.49	7.10	8.11	8.89	9.75	7.78	7.49	7.74
DIFFERENCE	.05	-.06	.03	.14	.19	.21	.26	.31
% DIFFERENCE	.80	-.81	.34	1.54	1.96	2.71	3.51	3.97
DEFL, FIXED NONRES INVEST (1972=100)								
PRESIDENTS TAX REFORM	222.2	234.6	244.6	254.4	265.0	275.3	285.9	297.7
BASELINE	222.1	233.9	243.5	253.0	263.3	272.9	282.9	294.0
DIFFERENCE	.1	.7	1.1	1.3	1.8	2.4	3.0	3.7
% DIFFERENCE	.1	.3	.4	.5	.7	.9	1.1	1.3

EFFECTS ON THE U.S. ECONOMY
OF IMPLEMENTING THE PRESIDENT'S TAX PLAN

	1986	1987	1988	1989	1990	1991	1992	1993
GROSS OUTPUT, AGRIC (BILL 72 $)								
PRESIDENTS TAX REFORM	114.3	114.7	117.4	119.3	115.5	121.6	123.0	123.9
BASELINE	113.9	114.2	116.5	118.3	115.2	121.2	122.4	123.7
DIFFERENCE	.4	.5	.9	1.0	.3	.4	.6	.2
% DIFFERENCE	.4	.4	.7	.8	.2	.4	.5	.2
GROSS OUTP DEFL, AGRIC (1972=100)								
PRESIDENTS TAX REFORM	224.5	236.5	243.2	255.5	271.5	285.0	298.8	315.1
BASELINE	224.9	237.7	244.3	254.8	269.7	284.0	299.1	314.9
DIFFERENCE	-.4	-1.2	-1.2	.7	1.8	1.0	-.3	.2
% DIFFERENCE	-.2	-.5	-.5	.3	.7	.4	-.1	.1
FARM EMPLOYMENT (MILL)								
PRESIDENTS TAX REFORM	3.074	2.976	2.917	2.845	2.648	2.658	2.576	2.500
BASELINE	3.068	2.968	2.903	2.834	2.655	2.668	2.580	2.500
DIFFERENCE	.006	.008	.013	.011	-.007	-.010	-.004	-.001
% DIFFERENCE	.187	.279	.456	.382	-.245	-.371	-.148	-.024
FARM INVESTMENT (BILL 72 $)								
PRESIDENTS TAX REFORM	6.1	6.2	6.4	6.5	5.9	5.9	6.3	6.7
BASELINE	6.1	6.3	6.5	6.8	6.6	6.7	6.8	7.1
DIFFERENCE	.0	.0	.0	-.3	-.7	-.7	-.5	-.4
% DIFFERENCE	-.2	-.2	-.7	-4.3	-10.6	-11.0	-7.9	-5.1
FARM INVESTMENT (BILL $)								
PRESIDENTS TAX REFORM	13.6	14.7	15.7	16.5	15.7	16.3	18.0	20.0
BASELINE	13.6	14.7	15.7	17.1	17.4	18.2	19.3	20.8
DIFFERENCE	.0	.0	.0	-.6	-1.7	-1.9	-1.3	-.8
% DIFFERENCE	-.1	.1	-.3	-3.8	-10.0	-10.2	-6.9	-3.8
USER COST OF CAPITAL, AGRIC (%)								
PRESIDENTS TAX REFORM	67.176	75.289	77.556	79.499	83.173	80.167	81.557	84.762
BASELINE	59.149	62.841	65.518	68.263	71.913	69.748	71.103	73.973
DIFFERENCE	8.027	12.448	12.038	11.237	11.260	10.420	10.453	10.789
% DIFFERENCE	13.570	19.809	18.374	16.461	15.657	14.939	14.701	14.585
PERS CONSUMP EXPS (BILL 72 $)								
PRESIDENTS TAX REFORM	1137.3	1170.9	1208.7	1246.1	1269.2	1310.2	1345.5	1377.5
BASELINE	1130.1	1160.3	1195.4	1231.4	1252.4	1293.2	1330.0	1364.4
DIFFERENCE	7.1	10.6	13.3	14.8	16.8	17.0	15.5	13.1
% DIFFERENCE	.6	.9	1.1	1.2	1.3	1.3	1.2	1.0
FIXED NONRES INVEST (BILL 72 $)								
PRESIDENTS TAX REFORM	232.1	248.3	261.1	272.8	267.4	288.6	301.2	311.1
BASELINE	232.5	251.5	266.6	279.5	274.4	296.0	308.5	318.9
DIFFERENCE	-.4	-3.2	-5.5	-6.7	-7.0	-7.4	-7.3	-7.8
% DIFFERENCE	-.2	-1.3	-2.1	-2.4	-2.6	-2.5	-2.4	-2.4

EFFECTS ON THE U.S. ECONOMY
OF IMPLEMENTING THE PRESIDENT'S TAX PLAN

	1986	1987	1988	1989	1990	1991	1992	1993
PERS CONS EXPENDS, FOOD (BILL 72 $)								
PRESIDENTS TAX REFORM	204.2	209.4	215.5	220.9	225.3	230.8	234.3	238.0
BASELINE	203.3	208.3	213.7	218.6	222.8	228.2	232.1	236.2
DIFFERENCE	.5	1.1	1.8	2.2	2.5	2.5	2.2	1.9
% DIFFERENCE	.2	.5	.9	1.0	1.1	1.1	1.0	.8
DISPOSABLE PERS INCOME (BILL 72 $)								
PRESIDENTS TAX REFORM	1247.2	1290.1	1329.5	1372.8	1392.9	1445.2	1483.9	1519.1
BASELINE	1235.3	1273.0	1310.6	1354.0	1371.6	1424.2	1466.1	1505.3
DIFFERENCE	11.9	17.1	18.9	18.8	21.2	21.0	17.8	13.9
% DIFFERENCE	1.0	1.3	1.4	1.4	1.5	1.5	1.2	.9